No. 14-___

IN THE

# Supreme Court of the United States

CPV POWER DEVELOPMENT, INC.,
EIF NEWARK, LLC,
*Petitioners,*

v.

PPL ENERGYPLUS, LLC, ET AL.,
*Respondents.*

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

## PETITION FOR A WRIT OF CERTIORARI


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

*Counsel for EIF Newark, LLC*

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

*Counsel for CPV Power Development, Inc.*


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## QUESTION PRESENTED

Under the Federal Power Act, 16 U.S.C. §§824 *et seq*., States retain authority over electricity and capacity purchases by local utilities. They cannot, however, impose the rates for those purchases; only the Federal Energy Regulatory Commission (FERC) can regulate interstate wholesale rates. Seeking three new power plants, New Jersey conducted a competitive procurement and directed its local utilities to enter into long-term contracts with the successful bidders, providing the stable revenue needed to induce the developers' investment and support the costs of construction. Under those contracts, if the developer's accepted bid price exceeds what the developer earns by selling the plant's capacity in the FERC-supervised auction, the utility pays the difference to the developer; if auction revenue exceeds the bid price, the developer rebates the difference to the utility. The payment or rebate is passed on to retail ratepayers.

> Where, as a result of a state-directed procurement, the contract price to build and operate a power plant is the developer's bid price, and may result in payments beyond what the developer earns selling the plant's capacity in the FERC-supervised auction, is the program "field preempted" as a State's attempt to set interstate wholesale rates?

## PARTIES TO THE PROCEEDINGS

Petitioners are CPV Power Development, Inc. (CPV), Appellant below and a Defendant-Intervenor in the district court, and EIF Newark, LLC, formerly known, and identified below, as Hess Newark LLC, Appellant-Intervenor below. The President and Commissioners of the New Jersey Board of Public Utilities (Board) were sued in their official capacities and were Defendants-Appellants below. Joseph L. Fiordaliso was a named Defendant-Appellant below and remains a Commissioner of the Board. Lee A. Solomon, named in his official capacity below, was the President of the Board at the time this litigation commenced, but no longer holds that position. He was replaced by Richard Mroz. Similarly, Jeanne M. Fox and Nicholas V. Asselta, named in their official capacities below, were Commissioners of the Board at the time this litigation commenced, but no longer hold those positions. Mary-Anna Holden, Dianne Solomon, and Upendra Chivukula are now Commissioners.

Respondents, Plaintiffs-Appellees in the court below, are: PPL EnergyPlus, LLC; PPL Brunner Island, LLC; PPL Holtwood, LLC; PPL Martins Creek, LLC; PPL Montour, LLC; PPL Susquehanna, LLC; Lower Mount Bethel Energy, LLC; PPL New Jersey Solar, LLC; PPL New Jersey Biogas, LLC; PPL Renewable Energy, LLC; Calpine Energy Services L.P.; Calpine Mid–Atlantic Generation, LLC; Calpine New Jersey Generation, LLC; Calpine Bethlehem, LLC; Calpine Mid–Merit, LLC; Calpine Vineland Solar, LLC; Calpine Mid–Atlantic Marketing, LLC; Calpine Newark, LLC; Exelon Generation Company, LLC; Genon Energy, Inc.; NAEA Ocean Peaking Power, LLC; PSEG Power, LLC; Atlantic City Electric Company; and Public Service Electric & Gas Company.

## RULE 29.6 STATEMENT

Petitioner CPV Power Development, Inc. is a wholly owned, direct subsidiary of Competitive Power Ventures Holdings, LLC. No publicly held company owns 10% or more of CPV Power Development, Inc.'s stock. No publicly held company owns 10% or more of the interests in Competitive Power Ventures Holdings, LLC. Competitive Power Ventures Holdings, LLC is 88.55% owned by Warburg Pincus Private Equity IX, L.P.

Petitioner EIF Newark, LLC, formerly known (and identified below) as Hess Newark LLC, is 100% owned by EIF-NEC, LLC, which does not issue stock. No publicly held company owns 10% or more of the interests therein.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued



MISCELLANEOUS AUTHORITIES

TABLE OF AUTHORITIES—Continued

## PETITION FOR A WRIT OF CERTIORARI

CPV Power Development, Inc. (CPV) and EIF Newark, LLC, respectfully seek a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

## OPINIONS BELOW

The opinion of the United States Court of Appeals for the Third Circuit is reported at 766 F.3d 241 (3d Cir. 2014) and reprinted at App.1a. The district court's opinion is reported at 977 F. Supp. 2d 372 (D.N.J. 2013) and reprinted at App.34a.

## JURISDICTION

This case was filed in the district court under 28 U.S.C. §1331, raising constitutional challenges to New Jersey's program supporting construction of several new power plants. The district court issued final judgment on October 25, 2013. That judgment was appealed pursuant to 28 U.S.C. §1291. The Third Circuit affirmed on September 11, 2014. This Petition is filed within the time allowed by this Court's Rule No. 13. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

## CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Supremacy Clause is reprinted at App.118a. Relevant provisions of the Federal Power Act are reprinted beginning at App.119a.

## INTRODUCTION AND SUMMARY

The Third Circuit's decision holding that the Federal Power Act (FPA) of 1935, 16 U.S.C. §§824 *et seq*., preempts New Jersey's directed procurement of several new power plants needed by that State

misconceives, and crucially alters, the division of state and federal responsibility under the FPA. It directly undermines the States' ability to direct and supervise electricity and capacity purchases by local utilities, and thus to meet their citizens' long-term electricity needs through traditional means: long-term ratepayer commitments to power plant developers that provide the reliable revenue stream needed to support the capital investment required to build a power plant.

Given the enormous up-front investment required to build a power plant, those commitments are critical. In 2013, less than 3% of new power plant construction proceeded without revenue-stabilizing, long-term commitments to power plant developers in place. Those commitments are typically in the form of long-term contracts between the developer and local utilities, or reflect construction by vertically-integrated utilities that both generate electricity and sell to consumers, with the assurance that they will recover their costs through retail rates.

Under the FPA, States have sole authority to regulate and directly support power plant construction, and to pass the construction costs on to retail customers. The Federal Energy Regulatory Commission (FERC) is expressly denied authority over power plant construction (or retirement). Therefore, the vitality of the Nation's energy infrastructure ultimately depends on targeted *state* support for new power plants, most usually—until this, and the similar Fourth Circuit case that it followed said no[1]—through long-term contracts

[1] See *PPL EnergyPlus, LLC v. Nazarian*, 753 F.3d 467 (4th Cir. 2014). Separate petitions for certiorari are being filed addressing that case, which raises the same issues.

providing the revenue stream necessary for power plant development. The Third Circuit's decision undermines the States' ability to support that infrastructure development.

New Jersey's legislature determined that New Jersey needed new power plants to serve several regions of the State. The State then conducted a procurement, offering successful bidders willing to build the needed plants long-term contracts with New Jersey's local utilities. Those contracts were designed to provide the stable revenue needed to support power plant construction.

To induce the bids and the capital investment of nearly three-quarters of a billion dollars needed to build even one new power plant, the New Jersey legislature determined to offer the successful bidders a financial arrangement called a "contract for differences," here offered through contracts known as Standard Offer Capacity Agreements (SOCAs). Under the SOCAs, the bidders agreed to build and operate the requested power plants and to sell the plants' capacity in the federally-supervised interstate capacity auction, according to the rules of that auction. The local utilities would pay the developer the *difference* between the developer's auction sales revenue and its bid price to build and operate the plant. If the developer's auction sales revenue exceeded the bid price, the developer would rebate the difference to the utilities. The utilities would then recover their costs from (or rebate surpluses to) their retail customers.

New Jersey's program is an exercise of its traditional powers. To ensure reliable electricity supply, New Jersey directed its local utilities to enter into long-term contracts at prices set by a competitive procurement. It promised the utilities that they would

recover their costs from retail customers. It did all this to spur construction of needed generation resources available to the State.

The FPA assigns FERC authority over interstate wholesale sales of electricity and interstate transmission. Congress expressly preserved state authority over electric generation, intrastate transmission, and electric sales and rates other than wholesale sales. States retain broad authority over local utilities. States have long exercised their authority over "utility buy-side" decisions to support power plant development by directing their utilities to buy power (or approving proposals to buy power) through long-term contracts that ensure reliable, economical electricity for their citizens.

Until the decision below—and the Fourth Circuit decision that it followed—not only the existence of state authority to direct such long-term contracts, but the *limits* of the States' authority to direct their utilities to enter into contracts, were clearly demarcated and well understood. States could mandate and oversee competitive procurements for local utilities, and direct them to enter into contracts at market prices established by those procurements. What States could *not* do was *set* the price at which utilities buy, or developers sell, energy or capacity. State price-setting would usurp FERC's exclusive authority.[2] The Third Circuit's field preemption theory improperly equates a competitive price, offered by a developer, with a price impermissibly imposed by the State. It thereby nullifies the States' power to direct local

[2] See *Cal. Pub. Utils. Comm'n*, 132 FERC ¶61,047, P 69 (2010), *clarified,* 133 FERC ¶61,059 (2010), *reh'g denied*, 134 FERC ¶61,044 (2011).

utilities to enter into contracts that meet their citizens' needs.

As shown below, the supplemental payments under the contracts for differences at issue were actually not rates subject to FERC's jurisdiction at all because they did not govern a sale of capacity or electricity. But even if one were to accept the premise that they were subject to FERC jurisdiction, that would not mean preemption. It would simply invite FERC's review of those rates at FERC's initiative or at the behest of anyone complaining about them. Rates or contracts subject to FERC's review cannot usurp FERC's jurisdiction. Indeed, by judicially declaring the contracts invalid, nominally to protect FERC's authority, the Third Circuit's decision paradoxically prevented FERC from exercising any authority it might have to review those contracts. What New Jersey did not do is *set* a wholesale rate at which energy or capacity is purchased. If the purchase price is not imposed by the State, but by the market, as a developer's competitive offer, it does not usurp FERC's rate-review authority, and is not "field preempted." The Third Circuit's contrary ruling misses this basic point, eviscerating boundaries within which States and FERC have operated for decades.

The Third Circuit's ruling equating a procurement with a rate set by the State undermines a tool widely used by States to stimulate construction and other energy initiatives. Directions to local utilities to buy electricity or capacity stimulate power plant construction and support other energy initiatives. The particular mechanism used here is especially useful. Maryland used a nearly identical approach to support

a power plant needed by that State.[3] That approach is well-suited to its purpose. A "guarantee" measured by the difference between what the developer bids to build a plant, and what it earns selling its capacity, effectively limits ratepayer contributions to the project.

The limitation imposed by the Third Circuit on the States' ability to support the Nation's electricity infrastructure is potentially devastating to the long-term health of that infrastructure because FERC itself lacks authority to authorize new power plant construction. At best, FERC has only an indirect role to play in stimulating power plant construction as an "incident" to its market and rate supervision.

A quarter century ago, the Court directed courts considering "field preemption" under the FPA's sister statute to "take seriously the lines Congress drew in creating a dual regulatory system," and avoid "extravagant" interpretations of federal energy regulatory jurisdiction at the States' expense. *Nw. Cent. Pipeline Corp. v. State Corp. Comm'n of Kan.*, 489 U.S. 493, 512-13 (1989). The Court also admonished that the inevitable interaction between state and federal initiatives should not be mistaken for preemptive conflict. *Id*. at 517-18. The Fourth Circuit's decision ignored the Court's directions. The Court should grant certiorari to address the important questions presented and restore the States' power to support needed energy infrastructure development.

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[3] See *Nazarian*, 753 F.3d at 473.

## STATEMENT

### A. The FPA Preserves the States' Power To Support Power Plant Construction

The "[n]eed for new power facilities, their economic feasibility, and rates and services, are areas that have been characteristically governed by the States." *Pac. Gas & Elec. Co. v. State Energy Res. Conservation & Dev. Comm'n*, 461 U.S. 190, 205 (1983). The FPA preserves each State's authority to ensure reliable electricity supply for its citizens by supporting power plant construction, transmission line approval, or through development of new technologies. It also preserves the States' authority to set retail rates to support those initiatives.

With the FPA, 16 U.S.C. §§824 *et seq.*, Congress vested exclusive regulatory authority over "sale of electric energy at wholesale in interstate commerce" in what eventually became FERC. 16 U.S.C. §824(a), (b)(1). FERC also has authority over practices "affecting," or "in connection" with, rates. 16 U.S.C. §§824d, 824e. But FERC's authority extends "only" to matters "not subject to regulation by the States." *Id.* §824(a). Moreover, FERC "shall not have jurisdiction, except as specifically provided . . . , over facilities used for the generation of electric energy . . . ." 16 U.S.C. §824(b)(1).

While the federal role has changed over time, "States retain significant control over local matters," including "utility generation and resource portfolios" and "utility buy-side . . . decisions," *i.e.*, where the utility purchases power to meet its needs rather than construct its own facilities. *New York v. FERC*, 535 U.S. 1, 24 (2002). In 2005, when Congress expanded FERC jurisdiction over transmission and reliability

standards, see 16 U.S.C. §§824o *et seq.*, it again denied FERC the authority "to order the construction of additional generation . . . capacity," 16 U.S.C. §824o(i)(2), confirming that "[n]othing in this section shall be construed to preempt any authority of any State to take action to ensure the safety, adequacy, and reliability of electric service within that State . . . ." *Id.* §824o(i)(3).

State support for power plant construction through supervision of local utilities and state-approved charges on retail ratepayers is, of course, nothing new. Under the classic regulatory model, with vertically-integrated utilities which both generate electricity and sell electricity to retail ratepayers, States ensured needed new power plant construction by allowing local utilities to recover prudently incurred costs from retail ratepayers. Many States continue to have vertically-integrated utilities. Others, like New Jersey, have partially restructured their electric power sector by requiring their local utilities to buy some or all of their generation requirements from the interstate markets, again with the costs of those purchases borne ultimately by retail ratepayers.

Even in restructured states, state regulators retain regulatory control over purchasing decisions by their local utilities, and the rates they charge their customers. States use that authority to direct those utilities to enter into long-term contracts to purchase power (or to approve such contracts). Those contracts assure reliable electricity supplies for state citizens. And they assure developers of the long-term revenue stream needed to finance projects costing hundreds of millions of dollars.

Almost all (more than 97%) new power plant construction rests on long-term commitments, underwritten by ratepayers. Those commitments typically take the form of long-term contracts between the developer and the regulated local utility (64%), or construction by the local utility that owns the power plant and sells to retail consumers (29.6%). Only 2.4% of recent new generation capacity was built "on spec," *i.e.*, relying solely on short-term open market sales.[4]

State authority to direct local utilities to buy power or capacity from prospective developers poses no conflict with federal law or policy. See 18 C.F.R. §35.27 (recognizing States' authority to "establish . . . [c]ompetitive procedures for the acquisition of electric energy . . . purchased at wholesale"). This includes the authority to "dictate the generation resources from which utilities may procure electric energy." *Cal. Pub. Utils. Comm'n*, 134 FERC ¶61,044, P 30 & n.62 (2011). If the resulting contracts are subject to FERC jurisdiction, FERC may review them.

What States may *not* do is set the price (rather than have the price set competitively) at which electricity or capacity is sold at wholesale. Only FERC can determine whether prices subject to its jurisdiction are just and reasonable. Compare *Midwest Power Sys., Inc.*, 78 FERC ¶61,067, 61,248 (1997); *Cal. Pub. Utils. Comm'n*, 132 FERC ¶61,047, P 69 (2010) (California

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[4] These figures are for 2013. See American Public Power Association, *Power Plants Are Not Built on Spec—2014 Update* at 1-2 and Table 1 (2014) *("2014 APPA Study")*, http://goo.gl/t62QuS. Similar figures are available for 2011. See American Public Power Association, *Power Plants Are Not Built on Spec: An Analysis of New Electric Generation Projects Constructed in 2011* at 5-6 and Table 2 (2012) *("2012 APPA Study")*, http://goo.gl/WCboHw.

statute "preempted to the extent that the [State] is setting wholesale rates"), with *Doswell Ltd. P'ship*, 50 FERC ¶61,251, 61,756-57 (1990) (approving state-certified agreement, with prices set by competition); *Commonwealth Atl. Ltd. P'ship*, 51 FERC ¶61,368 (1990).

### B. New Jersey's Initiative Supported Necessary Power Plant Construction

By 2010, electric rates in New Jersey were climbing, demand was growing, a raft of environmental regulations threatened to retire many older, higher-polluting power plants, and there were continuing reliability problems. Despite the evident need, the legislature observed that existing markets were not inducing investment in the construction of significant new generating resources for the State. As summarized by the court below, "New Jersey concluded that it needed more electric energy generators." App.15a.

In January 2011, the New Jersey legislature enacted the Long-Term Capacity Agreement Pilot Program (LCAPP) Act to meet the crisis.[5] That statute created incentives for the construction of "2,000 megawatts of capacity to the regional power grid from which New Jersey obtained its electrical energy." *Id*. The LCAPP Act directed the New Jersey Board of Public Utilities (Board) to oversee a competitive procurement to select up to 2,000 MW of new power plants. The Act also directed the Board to order New Jersey's local utilities to execute 15-year standard offer capacity agreements (SOCAs), assuring the successful bidders (the "SOCA

[5] N.J. Stat. Ann. §§48:3-51, 48:3-98.2-.4.

developers") a fixed level of revenue over the 15-year contract term.

Out of 34 bids, CPV's proposal to build a 663.4 MW natural gas-fired power plant in Middlesex County, New Jersey, at an expected cost of nearly three quarters of a billion dollars, was accepted. EIF Newark, LLC (formerly known as Hess Newark LLC)'s proposal to build a 625.0 MW natural gas-fired power plant in Essex County, New Jersey, was also accepted, as was the proposal of NRG Energy, Inc. to build a 680.1 MW plant. NRG's project was ultimately cancelled after NRG failed to clear the 2012 capacity auction in compliance with FERC's revised auction rules.

The SOCAs are financial agreements, operating as a hedge. The party at risk for the yearly market price fluctuations in capacity revenue (*i.e.*, the plant developer) trades that fluctuating revenue stream for a defined revenue stream, as determined by the developer's winning bid. It receives steady revenue, and the counterparty—the local utility—takes on the risk of fluctuating prices. The Third Circuit called these contracts a "guarantee." App.24a.

Each SOCA developer thus agreed to build and operate a power plant of a specified capacity, in a designated locale, and to sell the plant's capacity in the federally-supervised capacity auction, according to the FERC-approved auction rules.[6] In consideration, the

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[6] As a definitional matter, "capacity" is used in two related ways. Capacity is the quantity of electricity that a given resource can produce or make available. But because electricity demand fluctuates (and electricity cannot be stored), the ability to provide electricity on demand is itself sold in interstate markets. As the D.C. Circuit explained:

developer would receive revenue at its offer price, over 15 years. If the developer's revenues from selling capacity through the auction were below the contract price, New Jersey's utilities would pay the difference, and pass any cost on to their ratepayers. If the developer realized sales revenues above its yearly contract price, the developers would rebate the difference to the local utilities, which would pass the rebates on to retail ratepayers.

### C. FERC Can Influence Power Plant Development Only Indirectly Through Its Market and Rate Supervision

Under the FPA, FERC regulates interstate wholesale energy markets and has exclusive authority to determine whether rates are "just and reasonable." 16 U.S.C. §824d(a). FERC may also choose to regulate other matters "affecting" or "in connection with" rates. 16 U.S.C. §§824d, 824e. FERC has encouraged formation of "regional transmission organizations," which coordinate generators, transmission resources, and wholesale purchasers. PJM Interconnection, L.L.C. (PJM), spanning most of thirteen states, including New Jersey, is the largest of these entities.

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> "Capacity" is not electricity itself but the ability to produce it when necessary. It amounts to a kind of call option that electricity transmitters purchase from parties - generally, generators - who can either produce more or consume less when required. The penultimate and most proximate buyers of capacity (before the consumers who ultimately shoulder the costs in their utility bills) are . . . the public utilities that deliver electricity to end users.

See *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 479 (D.C. Cir. 2009) *("CDPUC")*.

Capacity is frequently bought and sold through bilateral contracts. See *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 171 (2010) ("The [FPA] allows . . . sellers and buyers [to] agree on rates by contract.").[7] Non-auction sales are subject to FERC's review for "justness and reasonableness," whether the result of state-directed procurements or not. Where the price is competitively set by a seller without market power, FERC's review is limited because market-based rates are presumed valid. See *Morgan Stanley Capital Grp., Inc. v. Public Util. Dist. No. 1*, 554 U.S. 527, 547-48 (2008).

As a supplement to the many other markets and methods for selling capacity, FERC has encouraged regional transmission organizations to operate forward markets for capacity sales. See, *e.g.*, *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 484 (D.C. Cir. 2009) *("CDPUC").* A forward market functions as a clearing house for purchases and sales, and can also generate "price signals" that may prompt investment in new plants (or retirement of old ones). See *New England Power Generators Ass'n, Inc. v. FERC*, 757 F.3d 283, 287 (D.C. Cir. 2014).

The D.C. Circuit approved FERC's development of organized forward capacity markets. See *CDPUC*, 569 F.3d at 484-85. FERC premised that approval by explaining that it was merely exercising its authority over wholesale prices and markets, which could incidentally spur power plant construction. Such incidental effects, the court said, would not displace or

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[7] Long-term contracts are central to the provision of reliable electric supply; the FPA is "premised" on them. *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968). They are a "key factor fostering stability in the electricity market, to the longrun benefit of consumers." *NRG*, 558 U.S. at 174.

invade the States' primary authority over power plant construction. *Id.*

PJM's auction, the Reliability Pricing Model (RPM), operates in conjunction with, and in no way displaces, the many other methods of buying and selling capacity in the region. PJM surveys the region to predict how much capacity will be needed three years hence. Almost all generators must offer their capacity—*including capacity that is already the subject of other contracts, at prices different than the auction price*—for one year, three years in the future. Offers to sell are stacked, lowest to highest. The clearing price is the highest price PJM must accept to acquire the capacity to meet projected demand. Offers above that price are rejected. Accepted offers are paid the clearing price, no matter what the actual offer was. PJM buys the accepted capacity, at the clearing price, and resells it to auction purchasers. *PPL EnergyPlus, LLC v. Nazarian*, 753 F.3d 467, 472-73 (4th Cir. 2014).

Almost all capacity is offered into this auction at "zero"—meaning that offerors are "price takers," selling at *whatever* clearing price the auction produces. That is because a power plant requires enormous up-front capital investment. Once those costs are sunk, the cost of supplying capacity is small, so a rational offeror wants to be paid something, rather than nothing, and will offer at a price certain to clear. Moreover, utilities that have already bought capacity under long-term contracts are required to participate in the auction, and will likewise offer that contracted capacity into the auction at zero.

Given the reasoning of the Third Circuit, it bears emphasis that the auction clearing price controls auction sales, but does not set a price for the plethora of transactions outside the auction. It is a "residual"

pricing model only. Much capacity offered into the auction is already subject to long-term bilateral contracts, under which local utilities (with the concurrence or at the direction of the State) buy capacity at negotiated or competitively bid prices, different from the auction price. FERC requires the owner of that capacity to offer it into the auction. In other words, the local utility buys capacity, long-term, and resells it at auction. The result is multiple prices for capacity, even capacity later sold through the auction.

The net economic effect of state-directed bilateral capacity purchase agreements is, of course, the same as that of the SOCAs at issue here: The local utility and its ratepayers absorb the difference between the long-term price under the SOCAs, and whatever the yearly auction price turns out to be.

### D. FERC Approved CPV and EIF's Sales Of Capacity Into the Auction

New gas-fired generators are barred from entering the auction as price-takers, and are instead required to clear their first (but not subsequent) auction with a minimum offer price, reflecting costs.

Until the 2012 auction, FERC had exempted state-supported generators from minimum offer price rules, allowing them to bid zero so that state-sponsored projects would receive the clearing price for their capacity. *N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74, 79, 86 (3d Cir. 2014) *("NJBPU")*. But in response to New Jersey's and Maryland's similar programs, FERC subjected state-supported generators to minimum offer price rules (to which they had formerly been exempted), but held that "even if discriminatory subsidies are being received, if the resource is needed at the [minimum offer price] then it . . . should be

permitted to participate in the auction regardless of whether it also receives a subsidy." *Id.* at 98, 111 (FERC "permit[ted] states to develop whatever capacity resources they wish, and to use those resources to any extent that they wish, while approving rules that prevent the state's choices from adversely affecting wholesale capacity rates.") (internal quotation marks omitted).[8]

CPV, EIF, and NRG offered their capacity into the 2012 auction according to these rules. CPV's and EIF's offers cleared; NRG's did not. FERC approved the clearing price. See *PJM Interconnection, L.L.C.*, 143 FERC ¶61,090, P 143 (2013). When NRG could not clear the auction under FERC's rules, it cancelled its project.

### E. The Decisions Below

Respondents include incumbent generators, competitors of the successful bidders in New Jersey, who claim that the additional competition from the successful bidders would affect their prices in the auction. Respondents also include the electrical local utilities that signed the SOCAs under protest. They brought this case in the United States District Court for the District of New Jersey against members of New Jersey's Board of Public Utilities. Some of the respondents also brought a parallel case challenging Maryland's similar subsidy program for one power plant, also owned by CPV. See *Nazarian,* 753. F.3d 467. Petitioner CPV intervened.

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[8] See *PJM Interconnection, L.L.C.*, 135 FERC ¶61,022, P 175 (2011) ("once a new resource has cleared in one auction at the offer price floor, the resource has demonstrated that it is . . . economic . . . and there is no reasonable basis for continuing to" set a price floor on bids).

Respondents asserted that the New Jersey initiative was both "field preempted" and "conflict preempted." They also alleged a Commerce Clause violation. The district court held for Respondents on "field preemption" and "conflict preemption," App. 106a, 108a-109a, declaring New Jersey's program invalid. It rejected Respondents' Commerce Clause challenge. App.111a.

CPV and the New Jersey defendants appealed. EIF (the other successful bidder), intervened on appeal.

At the request of the Third Circuit, FERC filed an *amicus* brief. In that brief, FERC *did not* endorse the field preemption theory pressed by Respondents and ultimately adopted by the Third Circuit, namely, that the SOCAs "essentially set[]" a wholesale rate. FERC theorized instead that preemption should be found simply because the new power plant construction that New Jersey had spurred with the SOCAs would "affect" rates subject to FERC jurisdiction. The Third Circuit rejected FERC's "affecting" theory as over-broad and as inconsistent with this Court's decisions holding that state practices that merely affect rates are not preempted. App.29a-30a.

The Third Circuit panel nonetheless affirmed the district court ruling on "field preemption" grounds. It held that because the SOCA developers did not "solely" receive the PJM auction payments, New Jersey "essentially sets a price for wholesale energy sales," thus invading FERC's exclusive jurisdiction. App.24a (internal quotation marks omitted).

## REASONS TO GRANT THE PETITION

The Third Circuit's ruling (and the ruling in the Fourth Circuit case, which it followed) dangerously restructure the federal-state division of authority under the FPA—dangerously because it displaces the only governmental authorities, the States, authorized to directly support new power plant construction. The decision disregards this Court's stringent standards for finding preemption within the framework of interlocking federal-state electricity regulation. It finds improper state rate-setting where the State set no rate. And it hobbles the States in structuring incentives for new power plant construction, as well as for clean and renewable energy initiatives.

The FPA itself left undisturbed the States' primary authority over power plant construction, over capacity and electricity purchasing decisions by state utilities, and over charges to the ratepayers to support those activities. In finding preemption based on a State's exercise of its traditional power to support needed power plant construction through long-term, rate-payer supported contracts with the State's local utilities, the decision below contradicts the very premise upon which the FPA allocated power between the States and FERC, and FERC initiated its regulation of future capacity auctions.

Though the Third Circuit sought to narrow its ruling, the broad theory of improper state rate-setting upon which the decision rests strikes at the core of the States' ability to support power plant construction through long-term contracts and rate-payer support. The legal premises of the decision are decidedly wrong, and the restructuring of state-federal authority dramatic.

Moreover, the practical future effects of the court's ruling, and the disabling threat it poses to the States' ability to support energy infrastructure, is, as shown below, even more pronounced. By curbing the use of state-directed contracts, at competitively determined prices, to encourage power plant construction and other energy initiatives, the decision will hobble the States' ability to assure the creation of reliable energy supplies to meet their citizens'—and, thus, the Nation's—energy infrastructure needs. Those needs cannot be directly addressed by FERC under the FPA; Congress left those matters to the States. For the reasons described below, the Court should grant certiorari to address the important question presented.

## I. THE DECISION BELOW CONFLICTS WITH THIS COURT'S PRECEDENTS AND THE STRUCTURE OF THE FPA

### A. The Decision Disregards The Standards For Finding FPA Preemption

All "pre-emption cases . . . start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996). The "[n]eed for new power facilities, their economic feasibility, and rates and services, are areas that have been characteristically governed by the States." *Pac. Gas & Elec.*, 461 U.S. at 205. The FPA expressly preserves state authority, and forecloses FERC authority, over such matters.

FERC has exclusive jurisdiction over interstate sales and rates. 16 U.S.C. §824(a)-(b). FERC has jurisdiction over matters affecting or in connection

with rates, as well. FERC is denied "jurisdiction, except as specifically provided in this subchapter . . . over facilities used for the generation of electric energy." 16 U.S.C. §824(b)(1).

The resulting system of "interlocking" state-federal responsibility impacts preemption standards. With respect to *field* preemption, this Court cautioned, in the context of the FPA's sister statute, the Natural Gas Act, against "an extravagant . . . mode of interpretation" of FERC's authority that would undermine powers reserved to the States.[9] *Nw. Cent.*, 489 U.S. at 512-13. State programs are not field preempted merely because they affect matters within FERC's jurisdiction, as they inevitably do. Field preemption is found only where the State enters the federal sphere, as by setting rates for or regulating interstate transactions, *id*., which New Jersey did not do here.

The Third Circuit's preemption ruling largely disregarded this Court's admonitions to avoid finding preemption in this field, and entirely ignored the presumption against preemption.

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[9] While *Northwest Central* interpreted the Natural Gas Act ("NGA"), the same principles apply under the FPA: Because the relevant provisions of the FPA and the Natural Gas Act are "in all material respects substantially identical," there is an "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes." *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981) (internal quotation marks omitted).

### B. The Third Circuit Misunderstood And Fundamentally Altered the FPA's Division of State-Federal Authority

The Third Circuit's rulings reflect basic misunderstandings about the FPA regulatory framework established by FERC and the FPA itself.

#### 1. The Third Circuit's "field preemption" theory improperly finds that the SOCA contracts contained rates set by the State

First, the contract payments the Third Circuit found objectionable are not "rates" subject to FERC's exclusive jurisdiction. Second, and more important, whether or not they are subject to FERC jurisdiction, they were not "set" by New Jersey, and therefore do not invade FERC's exclusive jurisdiction.

##### (a) The SOCAs do not contain rates subject to FERC review

FERC's rate-review jurisdiction is ordinarily "limited to contracts [] which directly govern[] the rate in a jurisdictional sale—providing for the rate in whole or in part, or specifying or embodying it, or setting forth rules by which it is to be calculated."[10] Financial payments separate from such sales are not rates subject to FERC's review.[11] Thus, the contracts do not fall within FERC's jurisdiction (and FERC has not

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[10] *Cal. Indep. Sys. Operator Corp. v. FERC*, 372 F.3d 395, 403 (D.C. Cir. 2004) (internal quotation marks omitted).

[11] See *Revised Pub. Util. Filing Requirements*, 97 FERC ¶61,317, *4-5 (2001); *N.Y. Mercantile Exch.*, 74 FERC ¶61,311, 61,986-87 (1996) (FERC has no jurisdiction over a futures contract that can be settled financially, unless the contract goes to delivery).

asserted jurisdiction)—though, as shown below, it would make no difference for preemption purposes if they did because the prices were not *set* by the State.[12]

New Jersey's local utilities do not purchase electricity or capacity under the SOCAs. Instead, they make supplemental payments to support the construction and operation of new power plants. The only capacity sale occurs when the SOCA developers bid into the PJM auction. If they clear, they receive a price for that capacity, determined solely by the auction conducted under FERC-approved rules. The SOCA payment structure simply utilizes the revenue received by the developer in the auction, for the sale of capacity in the auction, as the baseline for calculating the supplemental payment. That payment is made in consideration of something more, and different than, offering a single year of capacity in the auction, namely, building a power plant of specified capacity in a desired locale, and committing to provide that capacity over 15 years.

That the amount of the SOCA payment is calculated by reference to revenues that the developer receives selling in the auction does not distinguish it from any other financial hedge, over which FERC similarly lacks jurisdiction. Because the SOCA payments are determined by the developers' winning proposals to build the desired power plant, and not from a jurisdictional sale of capacity, the SOCAs do not fall within FERC's jurisdiction at all.

The Third Circuit could not quite say that the SOCAs actually set a price for a sale of capacity that

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[12] FERC might choose to assert jurisdiction because the contracts "affect," or are "in connection with," interstate rates. See 16 U.S.C. §§824d, 824e.

would fall within FERC's jurisdiction. Instead, citing the Fourth Circuit's conclusion that a contract for differences "'*functionally* sets the rate,'" App.25a (quoting *Nazarian*, 753 F.3d at 476) (emphasis added), the Third Circuit concluded that the SOCAs "*essentially* set[] a price for wholesale energy sales." App.24a (internal quotation marks omitted; emphasis added). The court's rationale was that SOCA developers receive or make additional payments, "not solely the auction price they would have otherwise received." *Id.*

But there is nothing unusual about the fact that the total yearly revenue received by the SOCA-supported developer is different than the auction price. The auction price is the price for transactions within the auction, not outside it. Much capacity sold in the auction is already subject to bilateral contracts at prices different from the auction price. Until the decision of the Third Circuit, and the similar decision of the Fourth Circuit, the auction price did not extend beyond the auction to control prices for any form of capacity transaction (let along transactions involving the construction of a power plant) outside the auction.[13]

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[13] Moreover, the Third Circuit's rationale that additional payments "effectively" set rates does not distinguish these payments from any of the forms of subsidy—from tax subsidies to "direct[] subsidi[es]"—that the Third Circuit sought to distinguish. App.26a n.4. These alternative subsidies might well have some role to play in infrastructure development. But it is clear that long-term contracts, which the Third Circuit found here to be improper state rate-setting, have actually (and, as this case demonstrates, effectively) been used, to support investment in power plant construction.

Significantly, in its amicus brief in the Third Circuit, FERC did not endorse the notion that the SOCAs actually set rates. Instead, FERC argued that the New Jersey procurement was preempted because the addition of a new power plant in the marketplace would affect competition and therefore "affect" auction rates. The Third Circuit, citing *Nw. Cent.*, 489 U.S. at 514 (that state actions affect federal markets cannot give rise to preemption), properly rejected FERC's position as wildly overbroad: "[T]he law of supply-and-demand is not the law of preemption." App.29a.

**(b) New Jersey set no rates**

As shown above, the SOCAs are not, in fact, subject to FERC's exclusive jurisdiction over interstate rates under 16 U.S.C. §824(a), (b)(1). Nor has FERC asserted jurisdiction over them as involving practices "affecting," or "in connection" with, wholesale rates under 16 U.S.C. §§824d, 824e.

But even if the SOCAs or the prices and payments therein were reviewable by FERC, that would not give rise to preemption. It would simply mean that they were subject to FERC review, at the behest of a complaining party, or on FERC's own initiative. Contracts subject to FERC review cannot usurp FERC authority.

Field preemption can be found only if the State has purported to exercise a power—the power to set or judge rates for interstate sales—reserved to FERC by the FPA. New Jersey has not done so. The Third Circuit, like the Fourth Circuit whose decision it followed, lost sight of this fundamental distinction.

What distinguishes a permissible long-term power purchase agreement, or other contract entered into at the direction of the State, from one that is preempted,

is whether the State has purported to exercise the power to actually mandate the rates at which interstate power is purchased, thereby exercising the type of governmental power possessed exclusively by FERC. Rather, the SOCA prices were established by CPV's winning bid in a competitive procurement to construct and operate new power plants. That New Jersey established the procurement to solicit these proposals does not make the procurement impermissible rate-setting. The difference between directing a purchase and setting a rate is fundamental to the federal-state division of authority under the FPA.

That is because it is well established that States retain authority over "resource planning and utility buy-side decisions," see *New York*, 535 U.S. at 24. States may thus direct utilities to buy capacity or energy under long-term agreements. See, *e.g.*, 18 C.F.R. §35.27 (FERC recognizing States' authority to "establish . . . [c]ompetitive procedures for the acquisition of electric energy"); see also *Cal. Pub. Utils. Comm'n*, 134 FERC at P 30 & n.62 (States may "dictate the generation resources from which utilities may procure electric energy.").

A State crosses the line into exclusive FERC territory not by directing utilities to enter into contracts reviewable by FERC, but only if it purports to mandate the price at which capacity is purchased, rather than allow it to be established by negotiation, or, as here, by competitive bid. The State exercises the kind of governmental power over rates reserved to FERC by the FPA only if it sets or reviews the rate for reasonableness. FERC's cases reflect this basic distinction. Compare *Allegheny Energy Supply Co.*, 108 FERC ¶61,082, PP 15, 20, 21 (2004) (approving a state procurement where competitively bid prices

"were binding. Winning bidders received the actual price in their offers . . . ."), with *Cal. Pub. Utils. Comm'n*, 132 FERC at P 64 (state-imposed rate is preempted); *Midwest*, 78 FERC at 61,246, 61,248 (state-directed procurement "preempted to . . . the extent [the State] set[s] rates for the wholesale sales of electric energy").

By conducting a procurement, without setting a price, New Jersey did not usurp any power reserved to FERC. The Third Circuit—like the Fourth, whose decision it followed—missed this basic point. In so doing, these two Circuits have eviscerated a clear line between permissible procurements and impermissible state rate-review, hobbling the States' ability to support needed power plant construction and other energy initiatives in the process.

By restricting States' options to incentivize new construction, the Third Circuit created a void that FERC cannot fill. While FERC's regulation of wholesale rates might *indirectly* affect new construction, FERC may not *directly* regulate or support it; only States can. In *CDPUC*, the D.C. Circuit concluded that as an incident to its supervision of capacity markets and prices FERC could influence new power plant construction. 569 F.3d at 484-85.[14] It did so on the explicit understanding that FERC's exercise of such incidental power could *not* displace the States, which retain "the right to forbid new entrants from providing new capacity, to require retirement of existing generators, to limit new

[14] See also *Electric Power Supply Ass'n v. FERC*, 753 F.3d 216, 222 n.2 (D.C. Cir. 2014) (FERC "incidentally incentivized construction of more generation facilities, which are subject to State control"); *NJBPU*, 744 F.3d at 96-97 (discussing *CDPUC*, 569 F.3d 477).

construction to more expensive, environmentally-friendly units, or to take any other action in their role as regulators of generation facilities without direct interference from [FERC]." *Id.* at 481. Yet the Third Circuit's decision in this case, holding that a state-directed procurement amounts to state rate-setting if it results in generators receiving prices different than the auction price, does just that, cutting deeply into this area of state authority.

## II. THE THIRD CIRCUIT'S DECISION DEPRIVES STATES—AND FERC—OF AUTHORITY NEEDED TO SUPPORT THE NATION'S ELECTRIC INFRASTRUCTURE

The Third Circuit's decision nullifies New Jersey's program for the construction of two power plants needed by that State. Maryland's similar initiative was nullified on a similar and equally doubtful basis. See *Nazarian,* 753 F.3d 467. But the importance of these decisions extends far beyond these vital power plants. As described above, the assurance of stable long-term revenue has always been necessary to attract capital to build new power plants, and it continues to be necessary. Thus, virtually all new power plant construction—more than 97%—is supported by long-term ratepayer commitments. In States without vertically-integrated utilities (where ratepayer commitment to offset prudently incurred costs follows routinely), new power plants will not be built—nor other energy initiatives pursued—without the revenue assurances provided by long-term contracts.[15]

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[15] In 2013, only 2.4 percent of new capacity was built solely for open sales into interstate markets. *2014 APPA Study* at 1-2 and

State authority to support needed infrastructure development by directing the purchasing decisions of its utilities is more critical than ever. A substantial portion of the Nation's coal-fired power supply is being retired. Environmental regulations and economic factors favoring natural gas over coal are driving the change.[16] The Department of Energy projects that 50 GW of the Nation's existing 310 GW of coal-fired generating capacity will be retired by 2020.[17] PJM estimates retirements of between 11 and 25 GW in the region,[18] and independent analyses indicate up to 21 GW of retirements by 2018.[19] Even more closures are likely in light of the Environmental Protection Agency's June 2014 proposed regulation calling on States to take the lead role in reducing carbon dioxide emissions from power plants.[20]

The long-term contract mechanism to support infrastructure development used here by New Jersey (and by Maryland, see *Nazarian*, 753 F.3d at 473-74) —a contract for differences—is especially important

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Table 1. And the vast majority of even that small proportion received some type of subsidy. *Id.* at 2.

[16] See PJM, *Coal Capacity at Risk for Retirement in PJM: Potential Impacts of the Finalized EPA Cross State Air Pollution Rule and Proposed National Emissions Standards for Hazardous Air Pollutants* at 10-15 (2011) *("2011 PJM Study")*.

[17] U.S. Energy Information Administration, *Annual Energy Outlook 2014* at IF-34 (Apr. 2014).

[18] See *2011 PJM Study* at 27-28.

[19] Onur Aydin, Frank Graves, and Metin Celebi, *Coal Plant Retirements: Feedback Effects on Wholesale Electricity Prices*, The Brattle Group (Nov. 2013).

[20] EPA, *Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units, Proposed Rule*, 79 Fed. Reg. 34,830 (Jun. 18, 2014).

because it is ideally suited to its purpose of providing ratepayer support for power plant construction. Ratepayers pay only what is needed to support the intended result (whether a new natural gas-fired power plant or a wind farm), net of what the developer earns anyway by selling its capacity in the interstate market.

Other States have used similar mechanisms to encourage *renewable* energy production and carry out other facets of electric resource planning. Connecticut, for example, used this mechanism to support renewable power projects.[21] And States similarly direct their local utilities to negotiate cost-based contracts with economically distressed power plants where loss of the power plant's capacity could negatively impact reliable electric supplies for the State.[22] Thus, the decision below has immediate implications for a range of initiatives already in place, beyond support for new, traditional fuel power plants.

Long-term contracts are particularly effective in supporting development of new technology and fuel diversity. Massachusetts established a program under which it ordered its utilities to enter into long-term contracts with renewable power developers.[23] Illinois sought to promote clean coal technology, and so used its procurement power to require its utilities

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[21] Conn. Pub. Act 13-303, Section 6 (2013).

[22] See Jeff Beattie, "New York Regulators Throw Lifeline to Exelon's Struggling Ginna Nuke," *HIS Energy Daily* (Nov. 17, 2014); see also Resolution E-4471, Pub. Utils. Comm'n of Cal. (Mar. 22, 2012) (state-directed procurement to support continued operations at a natural gas-fired power plant); "Calpine Executes Contracts for Sutter Energy Center With California Utilities," *Reuters* (May 7, 2012), http://goo.gl/tPq07o. (same).

[23] 2012 Mass. Legis. Serv., ch. 209, §35.

to enter into long-term power purchase agreements with a firm building the world's first zero emission coal-fired power plant.[24] Nevada,[25] Rhode Island,[26] and other States also rely on state-run procurements to secure the long-term contracts necessary to cover the enormous costs of power plant development.

To be sure, the Third Circuit declined to adopt the Fourth Circuit's expansive "conflict preemption" holding, which bars States from implementing "incentives" to power plant construction that differ from the auction's price incentives. Compare *Nazarian*, 753 F.3d at 478-79. But that only minimally narrows the scope of the Third Circuit's own ruling. The premise of the Third Circuit's decision is that by directing a local utility's buy-side decision through a competitive procurement, a State is thereby setting a rate different from the auction rate, and thus invading FERC's exclusive rate-review authority. That holding, in itself, prevents the States from employing one of their traditional, and certainly most effective, tools – the offer of long-term, ratepayer-supported contracts – to encourage investment in new power plants or to support other energy initiatives.

Moreover, there is nothing unusual—or preempted —about the fact that such long-term contracts produce prices different from auction prices. Almost all capacity, including capacity already subject to bilateral contracts at prices different from auction prices (whether state-directed or not), must be bid into

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[24] See *Commonwealth Edison Co. v. Ill. Commerce Comm'n*, 2014 IL App (1st) 130544 (2014).

[25] Nev. Rev. Stat. §704.7316.

[26] *In re Review of Proposed Town of New Shoreham Project*, 25 A.3d 482 (R.I. 2011).

the capacity auction. All such contracts, particularly long-term agreements, cre ate a price for capacity sold in the yearly auction that is not "solely the auction price." Cf. App.24a. The economic effect of long-term capacity purchase agreements on the parties, and on the auction, is the same as the SOCAs at issue here.

The Third Circuit urged that its decision could be read narrowly to preserve a range of alternative subsidies that States might use, from tax breaks to direct payments. Of course, those supposedly acceptable forms of subsidy would also provide state-directed financial support beyond whatever revenue the developer receives by selling its capacity in the FERC-supervised auction. But even assuming that such subsidies would be permissible and have some role to play in certain settings, the Third Circuit's failure to distinguish between the State directing a utility's "buy-side decision," and a State actually setting a price, undercuts a basic mechanism by which States have actually (and as this case demonstrates, effectively) been addressing their citizens' long-term energy needs: State directed long-term agreements at the developer's bid price.

Finally, while resting on the notion that preemption was necessary here to protect FERC's authority, the Third Circuit's ruling actually diminished that authority. By invalidating these contracts as "field preempted," the Third Circuit prevented FERC from reviewing them to determine whether they are just and reasonable.[27]

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[27] See *CPV Shore, L.L.C.*, *CPV Maryland, L.L.C.*, 148 FERC ¶61,096, PP 28-31 (2014) (FERC ruling that it could not review the contracts because the court declared them invalid).

## CONCLUSION

The petition should be granted.

Respectfully submitted.

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

*Counsel for EIF Newark, LLC*

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

*Counsel for CPV Power Development, Inc.*

November 26, 2014

# APPENDIX

**APPENDIX A**

PRECEDENTIAL

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

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No. 13-4330

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PPL ENERGYPLUS, LLC; PPL BRUNNER ISLAND, LLC; PPL HOLTWOOD, LLC; PPL MARTINS CREEK, LLC; PPL MONTOUR, LLC; PPL SUSQUEHANNA, LLC; LOWER MOUNT BETHEL ENERGY, LLC; PPL NEW JERSEY SOLAR, LLC; PPL NEW JERSEY BIOGAS, LLC; PPL RENEWABLE ENERGY, LLC; CALPINE ENERGY SERVICES L.P.; CALPINE MID-ATLANTIC GENERATION, LLC; CALPINE NEW JERSEY GENERATION, LLC; CALPINE BETHLEHEM, LLC; CALPINE MID-MERIT, LLC; CALPINE VINELAND SOLAR, LLC; CALPINE MID-ATLANTIC MARKETING, LLC; CALPINE NEWARK, LLC;EXELON GENERATION COMPANY, LLC; GENON ENERGY, INC.; NAEA OCEAN PEAKING POWER, LLC; PSEG POWER, LLC; ATLANTIC CITY ELECTRIC COMPANY; PUBLIC SERVICE ELECTRIC & GAS COMPANY

v.

LEE A. SOLOMON, in his official capacity as President of the New Jersey Board of Public Utilities; JEANNE M. FOX, in her official capacity as Commissioner of the New Jersey Board of Public Utilities; JOSEPH L. FIORDALISO, in his official capacity as Commission of the New Jersey Board of Public Utilities; NICHOLAS V. ASSELTA, in his official capacity as Commissioner of the New Jersey Board of Public Utilities;

CPV POWER Development, Inc.;

*Appellant*

*HESS NEWARK, LLC, Intervenor in USCA
*(Pursuant to Courts order entered
Novenmber 14, 2013)

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No. 13-4501

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PPL ENERGYPLUS, LLC; PPL BRUNNER ISLAND, LLC; PPL HOLTWOOD, LLC; PPL MARTINS CREEK, LLC; PPL MONTOUR, LLC; PPL SUSQUEHANNA, LLC; LOWER MOUNT BETHEL ENERGY, LLC; PPL NEW JERSEY SOLAR, LLC; PPL NEW JERSEY BIOGAS, LLC; PPL RENEWABLE ENERGY, LLC; CALPINE ENERGY SERVICES L.P.; CALPINE MID-ATLANTIC GENERATION, LLC; CALPINE NEW JERSEY GENERATION, LLC; CALPINE BETHLEHEM, LLC; CALPINE MID-MERIT, LLC; CALPINE VINELAND SOLAR, LLC; CALPINE MID-ATLANTIC MARKETING, LLC; CALPINE NEWARK, LLC;EXELON GENERATION COMPANY, LLC; GENON ENERGY, INC.; NAEA OCEAN PEAKING POWER, LLC; PSEG POWER, LLC; ATLANTIC CITY ELECTRIC COMPANY; PUBLIC SERVICE ELECTRIC & GAS COMPANY

v.

LEE A. SOLOMON, in his official capacity as President of the New Jersey Board of Public Utilities; JEANNE M. FOX, in her official capacity as Commissioner of the New Jersey Board of Public Utilities; JOSEPH L. FIORDALISO, in his official capacity as Commission of the New Jersey Board of Public Utilities; NICHOLAS V. ASSELTA, in his official

capacity as Commissioner of the New Jersey Board of Public Utilities;

CPV POWER DEVELOPMENT INC.;
HESS NEWARK, LLC.

LEE A. SOLOMON,
JEANNE M. FOX,
JOSEPH FIORDALISO,
NICHOLAS ASSELTA,

*Apellants*

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On Appeal from the United States District Court
for the District of New Jersey

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(D.C. No. 3-11-cv-00745)

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District Judge: Honorable Peter G. Sheridan

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Argued: March 27, 2014

Before: FUENTES and SHWARTZ, *Circuit Judges*, and ROSENTHAL, *District Judge*.*

(Opinion Filed: September 11, 2014)

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* Honorable Lee H. Rosenthal, U.S. District Judge for the Southern District of Texas, sitting by designation.

Richard F. Engel [Argued]
Lisa J. Morelli
Jennifer S. Hsia
Office of Attorney General of New Jersey
Department of Law & Public Safety
Division of Law
Richard J. Hughes Justice Complex
25 Market Street, P.O. Box 093
Trenton, NJ 08625

Alex Moreau
Office of Attorney General of New Jersey
124 Halsey Street
P.O. Box 45029
Newark, NJ 07102
*Counsel for Appellants Lee A. Solomon, Jeanne M Fox, Joseph Fiordaliso, and Nicholas V. Asselta in No. 13-4501*

Larry F. Eisenstat
Clifton S. Elgarten [Argued]
Richard Lehfeldt
Jennifer N. Waters
Crowell & Moring LLP
1001 Pennsylvania Avenue, N.W.
Washington, DC 20004
*Counsel for Intervenor-Appellant CPV Power Development*

Justin N. Kaftan
Richard M. Zuckerman [Argued]
Dentons US
1221 Avenue of the Americas
New York, NY 10020

Brian J. Molloy
Wilentz, Goldman & Spitzer
90 Woodbridge Center Drive, 8th Floor
Woodbridge, NJ 07095
*Counsel for Intervenor Hess Newark LLC*

Paul D. Clement [Argued]
Erin E. Murphy
Candice Wong
Bancroft PLLC
1919 M Street N.W., Suite 470
Washington, DC 20036
*Counsel for Appellees*

Philip J. Passanante
Pepco Holdings, Inc./Atlantic City Electric Co.
500 North Wakefield Drive
Newark, DE 19714
*Counsel for Atlantic City Electric Co.*

David Musselman
Essential Power, LLC
150 College Road West
Princeton, NJ 08540
*Counsel for Essential Power, LLC*

Robert C. Brady
William P. Deni, Jr.
Lawrence S. Lustberg
Justin T. Quinn
Gibbons
One Gateway Center
Newark, NJ 07102
*Counsel for Calpine Energy Services*

Sarah G. Novosel
Calpine Corporation
875 15th Street N.W., Suite 700
Washington, DC 20005
*Counsel for the Calpine Companies*

Darryl M. Bradford
Veronica Gomez
Exelon Corporation
10 South Dearborn Street, 49th Floor
Chicago, IL 60603

David W. DeBruin
Matthew E. Price
Jenner & Block LLP
1099 New York Avenue N.W., Suite 900
Washington, DC 20001
*Counsel for Exelon Generation Co., LLC*

Jesse A. Dillon
PPL Services Corp.
Two North Ninth Street
Allentown, PA 18101

David L. Meyer
Morrison & Foerster
2000 Pennsylvania Avenue N.W., Suite 6000
Washington, DC 20006
*Counsel for the PPL Companies*

Tamara Linde
Vaughn L. McKoy
PSEG Services Corp.
80 Park Plaza
Newark, NJ 07102

Shannen W. Coffin
Steptoe & Johnson LLP
1330 Connecticut Avenue N.W.
Washington, DC 20036
*Counsel for PSEG Power, LLC and Public Service Electric & Gas Co.*

John P. Coyle Duncan & Allen
1575 Eye Street, N.W., Suite 300
Washington, DC 20005

Pamela M. Silberstein
National Rural Electric Cooperative Association
4301 Wilson Boulevard
Arlington, VA 22203
*Counsel for Amici Appellants National Rural Electric Cooperative Association and American Public Power Association*

Delia D. Patterson
American Public Power Association
1875 Connecticut Avenue, N. W.
Suite 1200
Washington, DC 20009
*Counsel for Amicus Appellant American Public Power Association*

Susanna Chu
Kaye Scholer
901 15th Street, N.W.
Washington, DC 20005
*Counsel for Amici Curiae Vermont Public Service Board, Vermont Department of Public Service, Rhode Island Public Utilities Commission, New England Conference of Public Utilities Commissioners Inc., Maine Public Utilities Commission, Connecticut Public Utilities Regulatory Authority, Connecticut Officer of Consumer Counsel, Connecticut Department*

*of Energy and Environmental Protection, California Public Utilities Commission, and Attorney General of Connecticut*

Clare E. Kindall [Argued]
Office of Attorney General
10 Franklin Square
New Britain, CT 06051
*Counsel to Amicus Connecticut Public Utilities Regulatory Authority*

Jeffrey A. Lamken
Martin Totaro
MoloLamken
600 New Hampshire Avenue, N.W.,
The Watergate
Washington, DC 20037
*Counsel to Amicus Curiae NRG Energy Inc.*

Eugene Grace
American Wind Energy Association
1501 M Street
Washington, DC 20005
*Counsel to Amicus Appellant American Wind Energy Association*

Ashley C. Parrish
David G. Tewksbury
King & Spalding
1700 Pennsylvania Avenue, N.W., Suite 200
Washington, DC 20006
*Counsel to Amici Curiae Electric Power Supply Association & Edison Electric Institute*

Stefanie A. Brand
Office of Public Defender
Division of the Ratepayer Advocate
140 East Front Street
4th Floor, P.O. Box 003
Trenton, NJ 08625
*Counsel to New Jersey Division of Rate Counsel*

Karis A. Gong
John L. Shepherd, Jr.
Skadden, Arps, Slate, Meagher & Flom
1440 New York Avenue, N.W., Room 10-6
Washington, DC 20005
*Counsel to Amicus Curiae PJM Power Providers Group*

Adam D. Chandler
U.S. Department of Justice
Appellate Section
950 Pennsylvania Avenue, N.W., Room 3312
Washington, DC 20530
Robert H. Solomon [Argued]
Federal Energy Regulatory Commission
888 1st Street, N.E.
Washington, DC 20426
*Counsel to Amici Curiae Federal Energy Regulatory Commission and the United States of America*

James P. Melia
Aspassia V. Staevska
Kenneth R. Stark
Pennsylvania Public Utilities Commission
400 North Street
Keystone Building
Harrisburg, PA 17120
*Counsel to Amicus Appellee Pennsylvania Public Utility Commission*

FUENTES, *Circuit Judge*.

Dissatisfied with the stock and reliability of power-generating facilities in New Jersey, the state adopted the Long Term Capacity Pilot Program Act. The Act—known as LCAPP—instructed New Jersey's Board of Public Utilities to promote the construction of new power-generating facilities in the state. Rather than pay for the construction of these plants directly, the Board of Public Utilities crafted a set of contracts, called Standard Offer Capacity Agreements, that assured new electric energy generators fifteen years of revenue from local utilities and, ultimately, New Jersey ratepayers. LCAPP guaranteed revenue to new generators by fixing the rates those generators would receive for supplying electrical capacity, that is, the ability to make energy when called upon.

The federal government, however, has exclusive control over interstate rates for wholesales of electric capacity. So when New Jersey arranged for LCAPP generators to receive preferential capacity rates, the state entered into a field of regulation beyond its authority. Accordingly, federal law preempts, and thereby invalidates, LCAPP and the related Standard Offer Capacity Agreements. We, therefore, affirm the District Court's judgment.

Although we affirm, we address our opinion to the field of interstate rates, and not to electric energy markets generally. Moreover, because we determine that LCAPP has been field preempted, we do not reach the conflict preemption and dormant Commerce Clause arguments raised by the parties.

## I. Background of the Case

This case concerns New Jersey's authority to arrange for the construction of new electric generators through a scheme focused on capacity prices. New Jersey's legislation, and its reasons for pursuing it, make sense only in the broader context of the regional energy market. Our analysis begins there.

### A. Regulatory framework

Electric energy generation and transmission occur in a complex regulatory environment populated with multiple private and public actors operating under the supervision of both state and federal agencies. The Federal Power Act embodies Congress's attempt "to reconcile the claims of federal and of local authorities and to apportion federal and state jurisdiction over the industry." *Conn. Light & Power Co. v. Fed. Power Comm'n*, 324 U.S. 515, 531 (1945).

#### *1. Both the federal government and the states regulate aspects of the electric energy system.*

With the Federal Power Act, Congress placed "the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce" under federal control. 16 U.S.C. § 824(a). Through the Act, Congress exercised its Commerce Clause prerogative to regulate matters of interstate commerce that the states could not. *Cf. Public Util. Comm'n of R.I. v. Attleboro Steam & Elec. Co.*, 273 U.S. 83, 89-90 (1927) (holding that the regulation of wholesale energy transactions that are "fundamentally interstate from beginning to end" may come only from the "exercise of the power vested in Congress."). And Congress further extended federal authority to those electric energy matters indirectly related to interstate commerce that had previously been subject

to state regulation. *See New York v. F.E.R.C.*, 535 U.S. 1, 6 (2002).

But Congress preserved state authority over many aspects of the electric energy industry. The Federal Power Act disclaimed any attempt to regulate "any other sale of electric energy" and declared that federal regulators "shall not have jurisdiction, except as specifically provided . . . over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce." 16 U.S.C. § 824(b)(1). So while the federal government has exclusive control over interstate rates and transmission, the "[n]eed for new power facilities, their economic feasibility, and rates and services, are areas that have been characteristically governed by the States." *Pac. Gas & Elec. Co. v. State Energy Res. Conservation & Dev. Comm'n*, 461 U.S. 190, 205 (1983).

*2. FERC has exclusive authority over interstate capacity sales and transmissions, and it has exercised that authority through regional transmission organizations.*

With respect to electric energy sales and transmissions, the federal government has placed one agency in charge of implementing the Federal Power Act, the Federal Energy Regulatory Commission. This agency, known as FERC, "regulates the sale of electricity at wholesale in interstate commerce." *Entergy La., Inc. v. La. Pub. Serv. Comm'n*, 539 U.S. 39, 41 (2003). FERC's jurisdiction over interstate wholesale rates is exclusive. *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966 (1986). Accordingly, FERC alone has the responsibility to "ensure that wholesale rates are just and reasonable."

*Entergy La., Inc.*, 539 U.S. at 41 (quotation marks omitted); 16 U.S.C. § 824d(a).

While FERC once directly considered whether the wholesale rates submitted to it were "just and reasonable," the agency has since moved away from this approach. Now FERC favors using market mechanisms to produce competitive rates for interstate sales and transmissions of energy. As part of this approach, FERC oversees regional transmission organizations that facilitate market operations.

PJM Interconnection LLC operates as the federally regulated regional transmission organization for the PJM region. PJM takes its name from "Pennsylvania," "Jersey," and "Maryland," the home states of the first utilities to pool their excess power and capacity in 1927. Today, the PJM region encompasses all or part of thirteen states and the District of Columbia, including the entirety of New Jersey. PJM operates the largest centrally dispatched power market in the world.

As a regional transmission organization, PJM has two responsibilities of significance to this case. First, PJM manages the flow of electric energy throughout the regional power grid, "dispatching" energy in real time to where it is needed. App'x 32. Second, PJM facilitates the interstate sales of electricity products, including energy and capacity, by managing marketplaces where those products may be exchanged. Electric energy is "the actual electricity that electric generators produce and which residential and business customers ultimately use." App'x 35 (quotation marks omitted). By contrast, electric capacity is "the ability to produce [energy] when called upon." App'x 36 (quotation marks omitted). In a system, such as PJM, where multiple power

generators pool their power, capacity describes the total amount of electricity-generating resources available for use. In other words, capacity is to energy what parking spaces are to cars—a measure of how much traffic the system can accommodate.

*3. New Jersey has moved away from a monopoly model for electric power generation and toward a market-based model approach.*

New Jersey once followed a traditional utility model, regulating local monopolies that both generated and distributed power to an exclusive service area. In 1999, however, New Jersey enacted the Electric Discount and Energy Competition Act, N.J. Stat. § 48:3-49 *et seq*. The Act restructured New Jersey's electric energy system so "customers would have the right to choose their electricity suppliers" and so that energy suppliers could obtain their energy from wholesale energy markets. App'x 44; *see also* N.J. Stat. § 48.3-50. To this end, New Jersey divorced the entities that generate electricity from those that supply it.

The change produced a delicate circuitry of interdependence between private entities and public utilities, and between New Jersey and federally-regulated wholesale energy markets. Generators, such as coal-fired or natural gas power plants, sell their capacity and energy to PJM through various PJM auctions. Load-serving entities pay PJM for furnishing capacity and energy, and, in turn, sell energy to consumers.[1] Electricity distribution companies, acting

[1] In New Jersey, customers may choose between numerous energy suppliers. The major electricity suppliers include Atlantic City Electric, Jersey Central Power & Light, Rockland Electric, and Public Service Electric & Gas.

as common carriers, use their network of power lines to transfer energy from generators to consumers.

Although New Jersey restructured its approach to electric energy regulation, it did not cede its "authority over the siting and construction of power plants." App'x 44. New Jersey's state utility regulator, the Board of Public Utilities, retained statutory authority for "general supervision and regulation of and jurisdiction and control over all public utilities." N.J. Stat. § 48:2-13(a). Pursuant to this authority, New Jersey has, for example, asserted jurisdiction over "[t]he charges assessed to customers for basic generation service," *id*. § 48:3-57(a)(1), and the licensing of electric power suppliers, *id*. § 48:3-78.

B. New Jersey passed LCAPP to encourage the construction of new power plants.

Roughly a decade after New Jersey restructured its electric power industry, New Jersey's legislature foresaw crisis. The legislature found that "New Jersey is experiencing an electric power capacity deficit and high power prices." N.J. Stat. § 48:3-98.2(e). The legislature warned that, "[a]s a result of a lack of new, efficient electric generation facilities, New Jersey has become more reliant on coal-fired power plants." *Id*. § 48:3-98.2(f). And the legislature specifically found that PJM's capacity market "has not resulted in large additions of peaking facilities or any additions of intermediate or base load resources available to the region and the State." N.J. Stat. § 48:3-98.2(b). New Jersey concluded that it needed more electric energy generators.

New Jersey's legislature enacted LCAPP in January 2011 to address its concerns. *See id*. § 48:3-98.3.

LCAPP aimed to encourage power generation companies to construct new power plants in New Jersey in order to add a cumulative 2,000 megawatts of capacity to the regional power grid from which New Jersey obtained its electrical energy. *Id*. § 48.3- 98.3(c)(1).

The legislature fostered additional electric generation in New Jersey by furnishing new generators with fifteen-year contracts to supply a predetermined amount of capacity at a predetermined rate. LCAPP authorized the Board of Public Utilities to compel electricity distribution companies to sign these contracts. Broadly speaking, these contracts, known as Standard Offer Capacity Agreements, guaranteed new generators a fixed level of revenue over a fifteen-year contract term.

Pursuant to LCAPP, the Board of Public Utilities solicited bids from power generation companies willing and able to construct new electric power generation facilities. N.J. Stat. § 48:3-98.3(a)-(b). The Board received bids from thirty-four companies to participate in LCAPP, and it selected the proposals of appellant CPV Power Development, Inc., intervenor-appellant Hess Newark LLC, and amicus NRG Energy, Inc. The Board then exercised its authority to compel the New Jersey electricity distribution companies to sign Standard Offer Capacity Agreements with the LCAPP generators. Since then, Hess's and CPV's projects have moved forward; NRG's project has not.

C. Proceedings to date

After New Jersey enacted LCAPP, several existing electrical energy generators and two electricity distribution companies filed suit against the Commissioners of the Board of Public Utilities. They

sought both a declaration that the Federal Power Act preempted LCAPP and an injunction prohibiting New Jersey authorities from enforcing LCAPP.

CPV intervened to defend the law a few months later. The District Court denied both sides' motions for summary judgment. Over thirteen days, the parties tried their case to the bench. Witnesses included experts on the electric energy industry, including former regulators and corporate executives. The trial concluded with a lengthy written opinion and a judgment in favor of the plaintiffs. *See PPL EnergyPlus, LLC v. Hana*, 977 F. Supp. 2d 372 (D.N.J. 2013); App'x 92-94.

The District Court determined that the Federal Power Act preempted LCAPP. The Court concluded that LCAPP infringed on FERC's exclusive control over the price received for interstate sales of capacity. Thus, LCAPP had been field preempted. The District Court further determined that LCAPP interfered with PJM's method of determining the price of capacity. Thus, LCAPP had been conflict preempted. Finally, the District Court rejected the plaintiffs' dormant Commerce Clause attack on the grounds that they had not met their burden of proof. Based on its conclusions, the District Court declared LCAPP unconstitutional, invalidated the Standard Offer Capacity Agreements, and enjoined New Jersey from enforcing the statute.

The Board of Public Utilities and CPV appealed. Hess Newark has since intervened in CPV's appeal.[2]

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[2] This Court granted Hess Newark's motion to intervene and consolidated the various proceedings. *See* Order dated Nov. 14, 2013, Case No. 13-4330 (granting Hess Newark's motion to intervene); Order dated Dec. 13, 2013, Case No. 13-4330

Each side has been joined on appeal by numerous amici. At the Court's invitation, the United States and FERC, acting amicus curiae, also briefed the preemption questions in support of the appellees.

II. Jurisdiction and Standard of Review

Because of the Constitutional claims presented in the case, the District Court properly exercised subject matter jurisdiction pursuant to 28 U.S.C. § 1331. Because the District Court entered final judgment, we exercise appellate jurisdiction pursuant to 28 U.S.C. § 1291.

"When the district court decides a constitutional claim based on a developed factual record, we exercise plenary review of the district court's legal conclusion. We defer to the factual findings supporting that conclusion unless they are clearly erroneous." *United States v. Voigt*, 89 F.3d 1050, 1064 (3d Cir. 1996) (citation omitted).

III. Discussion

Congress has distinguished between those matters that belong exclusively to the federal government, such as regulation of interstate sales and transmissions of energy, and those matters that remain within the regulatory authority of the states, such as the regulation of energy generators. *See* 16 U.S.C. § 824(b).

In the American system of federalism, federal law commands primacy over state law. The "Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of

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(consolidating Cases No. 13-4394 and No. 13-4501 with Case No. 13-4330)

the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. art. VI, cl. 2. As between state and federal law, therefore, any state law that "interferes with or is contrary to federal law . . . must yield." *Free v. Bland*, 369 U.S. 663, 666 (1962) (citing *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 210 (1824)).

Accordingly, if LCAPP intrudes into the exclusively federal field or conflicts with valid federal regulation, federal law preempts its effect and renders it invalid. *See Farina v. Nokia Inc.*, 625 F.3d 97, 115 (3d Cir. 2010). If, on the other hand, LCAPP addresses a local matter and leaves federal law unimpaired, it remains valid. *See id*. "Pre-emption analysis requires us to compare federal and state law." *PLIVA, Inc. v. Mensing*, 131 S. Ct. 2567, 2573 (2011). We do so with "the basic assumption that Congress did not intend to displace state law." *Farina*, 625 F.3d. at 116 (alteration omitted) (quoting *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981)). Only a clear and manifest conflict with federal law, or clear and manifest Congressional intent to override state choices, will overcome the presumption against preemption. *Id*. at 117.

A. Comparing LCAPP's subject matter to the federal regulation of interstate sales and transmissions of energy

The core of this case concerns field preemption, specifically whether LCAPP has strayed into the exclusive federal area of interstate wholesale rates. This begs the question of what the federal government and New Jersey have each regulated. Accordingly, within the broader framework described in Part I, we must fill in some of the details of PJM's FERC-

approved approach to setting market prices and LCAPP's design to incentivize the construction of new electric generators.[3] In practice, FERC, through PJM, regulates aspects of interstate wholesale rates through a capacity auction, while LCAPP encourages the construction of new generators by arranging for a capacity price supplement. We determine that LCAPP effectively sets capacity prices and therefore regulates the same field occupied by FERC.

*1. Through regional transmission organizations, FERC uses market mechanisms to price and sell electric capacity.*

Although the Federal Power Act speaks to interstate wholesales of electric energy, "the wholesale price for capacity . . . is squarely, and indeed exclusively, within FERC's jurisdiction." *N.J. Bd. of Pub. Utils. v. F.E.R.C.*, 744 F.3d 74, 97 (3d Cir. 2014). FERC has determined that "maintaining adequate resources" bears "a significant and direct effect on" wholesale rates. *PJM Interconnection, L.L.C.*, 119 FERC ¶ 61318, at 40 (2007). Therefore, FERC regulates interstate sales of electric capacity as part of its approach to regulating electric energy rates. *See Utilimax.com, Inc. v. PPL Energy Plus, LLC*, 378 F.3d 303, 305 (3d Cir. 2004).

FERC has approved PJM's Reliability Pricing Model as the means to set the interstate wholesale price for electric capacity in the PJM region. The Reliability

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[3] We recite the factual details necessary to decide the preemption question before us, resting on the careful factual findings of the District Court. In a related case, our Court described the federal and state regulatory schemes in greater detail. *See generally N.J. Bd. of Pub. Utils. v. F.E.R.C.*, 744 F.3d 74 (3d Cir. 2014).

Pricing Model attempts to match supply of capacity to demand for capacity. To calculate demand, PJM uses data from market participants and sophisticated computer models. To calculate supply, PJM uses two mechanisms. First, PJM tabulates all generation capacity within the PJM region that has been prearranged between suppliers and users of energy. This includes, for example, capacity associated with state-run monopolies or capacity privately exchanged between load-serving entities and energy generators. Second, PJM uses an auction to obtain the additional capacity needed to meet projected demand. The winners of the auction agree to provide capacity to PJM. *See generally* PJM Capacity Market Operations, PJM Manual 18: PJM Capacity Market §§ 3 ("Demand in the Reliability Pricing Model"), 4 ("Supply Resources in the Reliability Pricing Model") (21st ed. 2014).

The Reliability Pricing Model is a forward market and focuses on the capacity to be demanded and supplied for a one-year period beginning three years in the future. For example, the 2014-2015 Model settled capacity obligations for 2017-2018. And if the model has functioned properly, in three-years' time PJM will have contracted with enough capacity providers to satisfy the peak demand for capacity during 2017-2018.

Within the Reliability Pricing Model, the Base Residual Auction establishes the price capacity providers will receive for residual capacity supplied to PJM. Providers propose an amount of capacity they will offer to PJM, say 1,000 megawatt-hours per day, and the price at which they will offer that capacity, say $500 per megawatt per day. PJM orders these bids from lowest in price to highest in price. PJM then

accepts bids, starting with the lowest-price bid, until the cumulative capacity it has accepted satisfies PJM's auction goal. At that point, PJM rejects all other bids. The price of the last accepted bid becomes the price PJM will pay for all accepted auction bids. For example, if the $500 bid is the last one needed to satisfy demand, for example, $500 becomes the auction "clearing price." App'x 48.

*2. New Jersey, through LCAPP and the Standard Offer Capacity Agreements, has legislated what rates LCAPP generators will receive for their sales of capacity.*

By design, LCAPP focuses on capacity and capacity prices. Recall that the contracts here are standard offer *capacity* agreements contemplated by the Long Term *Capacity* Agreement Pilot Program. *See* N.J. Stat. § 48:3-51. And the Standard Offer Capacity Agreement price—referred to as the Standard Offer Capacity Price—is "the capacity price that is fixed for the term of the [agreement] and which is the price to be received by eligible generators under a board-approved [agreement]." *Id*.

New Jersey's legislature charged the Board of Public Utilities with implementing LCAPP to achieve New Jersey's stated policy goal of providing long-term price assurance to new energy generators. *See id*. § 48:3-98.3(c)(4). The Board did so by focusing on capacity and capacity prices:

- First, the Board "awarded" each generator a specific amount of capacity to transact through its Standard Offer Capacity Agreement.
- Second, the Board required generators to "participate in and clear" PJM's annual capacity auction. N.J. Stat. § 48:3-98.3(c)(12). Thus, when

NRG's bid failed to clear the PJM auction, its LCAPP participation ended.

- Third, the Board guaranteed each generator a fixed price for its cleared capacity. The Board achieved this by attempting to structure the Standard Offer Capacity Agreements as contracts-for-differences between the price of capacity received by a generator from the PJM auction and a price fixed by the Agreement itself. If the Agreement price exceeded the auction price, the Agreement required the electricity distribution companies to pay the difference in price, multiplied by the amount of capacity, to the LCAPP generators. If the auction price exceeded the Agreement price, the Agreement obliged the LCAPP generators to pay the difference in price, multiplied by the amount of capacity, to the electricity distribution companies.

In practice, the Standard Offer Capacity Agreements offered financial assurance to LCAPP generators: for a fixed amount of capacity, generators would receive a fixed price. And the Agreements extended these assurances for a fifteen-year term, with the price increasing each year.

*3. Both FERC, through PJM, and New Jersey attempt to regulate electric capacity prices and sales.*

FERC, acting through PJM, uses the Base Residual Auction to fix the capacity price electric generators will receive for the capacity they sell through PJM. At the same time, New Jersey, through LCAPP, has legislated that LCAPP generators will both receive the federal price for interstate capacity sales and also

receive an additional amount fixed by the BPU. Both efforts regulate electric capacity prices and sales.

We determine that LCAPP, through the Standard Offer Capacity Agreements, attempts to regulate the same subject matter that FERC has regulated through PJM's Reliability Pricing Model. The Agreements guarantee LCAPP generators a "multiyear pricing supplement" to raise the prevailing capacity price to an amount of New Jersey's liking. App'x 59. Indeed, New Jersey regulated the Standard Offer Capacity Rates precisely because the legislature believed that PJM's market-based incentives had failed to encourage new electric generators to construct adequate electric generation facilities. N.J. Stat. § 48:3-98.2(b). LCAPP builds on PJM's capacity prices.

Accordingly, New Jersey misses the mark when it argues that each Standard Offer Capacity Agreement represents "a contract for differences, functioning like a hedge" and, therefore, does not transact in capacity. *See*, *e.g.*, CPV Br. 39. True, LCAPP's price assurance insulates LCAPP generators from market volatility and thus eliminates their risk. But the Agreements provide more than risk-hedging; they provide for the supply and sale of capacity, as well. LCAPP commands generators to sell capacity to PJM. In return, New Jersey's statute ensures that the generators will receive the Standard Offer Capacity Rate for each quantity of capacity offered at auction and not solely the auction price they would have otherwise received. Accordingly, we agree with the District Court that "the Board essentially sets a price for wholesale energy sales" for LCAPP generators. App'x 78; *accord PPL EnergyPlus, LLC v. Nazarian*, 753 F.3d 467, 476 (4th Cir. 2014) (determining that a Maryland initiative

similar to LCAPP "functionally sets the rate that [a generator] receives for its sales in the PJM auction").

Anticipating this result, LCAPP's defenders contend that if the Standard Offer Capacity Agreements set capacity prices then the law would not be preempted because the reasonableness of the Agreement's rates would be within FERC's exclusive jurisdiction to review. True, FERC has jurisdiction over certain contracts that set rates between market participants. *See NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 171 (2010). But this argument conflates the inquiry into LCAPP's field of regulation with an inquiry into the reasonableness of the Standard Offer Capacity Rates. Here, whether the Standard Offer Capacity Agreements pick "just and reasonable" capacity prices is beside the point. What matters is that the Agreements have set capacity prices in the first place.

B. Because New Jersey has legislated in an exclusively federal field, its law must give way.

Because FERC has exercised control over the field of interstate capacity prices, and because FERC's control is exclusive, New Jersey's efforts to regulate the same subject matter cannot stand. "Where Congress has delegated the authority to regulate a particular field to an administrative agency, the agency's regulations issued pursuant to that authority have no less preemptive effect than federal statutes, assuming those regulations are a valid exercise of the agency's delegated authority." *Fellner v. Tri-Union Seafoods, L.L.C.*, 539 F.3d 237, 243 (3d Cir. 2008). Here, FERC's use of the Base Residual Auction to set interstate capacity prices is a lawful exercise of its authority. *See N.J. Bd. of Pub. Utils.*, 744 F.3d at 97. Indeed, only FERC has the authority to set interstate

capacity prices. *Id*. So the Federal Power Act, as administered by FERC, preempts and, therefore, invalidates, state intrusions into the field. *Cf. Fid. Fed. Say. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 153 (1982). New Jersey's regulations must yield.

LCAPP's defenders respond that New Jersey's interference with capacity prices does not trigger preemption because it is a lawful exercise of the state's authority to promote new generation resources. New Jersey does have authority over local energy matters, including the construction of power plants. *See*, *e.g*., *So. Cal. Edison Co. & San Diego Gas & Elec. Co*., 71 FERC ¶ 61,269, at 3 (1995). But LCAPP incentivizes the construction of new power plants by regulating the rates new electric generators will receive for their capacity. New Jersey could have used other means to achieve its policy goals.[4] Because Congress has evinced its intent to occupy the entire field of interstate capacity rates, however, New Jersey's reasons for regulating in the federal field cannot save its effort: "any state law falling within that [federal] field is preempted." *Silkwood v. Kerr-McGee Corp*., 464 U.S. 238, 248 (1984).

That New Jersey has attempted to regulate federal matters for local purposes also distinguishes its situation from *Northwest Central Pipeline v. State Corp. Commission of Kansas*, 489 U.S. 493, 512-13

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[4] For example, permissible means may include "utilization of tax exempt bonding authority, the granting of property tax relief, the ability to enter into favorable site lease agreements on public lands, the gifting of environmentally damaged properties for brownfield development, and the relaxing or acceleration of permit approvals." App'x 74. New Jersey may also directly subsidize generators so long as the subsidies do not essentially set wholesale prices.

(1989). There, the U.S. Supreme Court rejected the argument that Kansas overstepped its authority to regulate the gathering of natural gas by promulgating rules that, if enforced, would indirectly affect interstate rates. *Id*. at 512-14. By contrast, LCAPP does not regulate the construction of new power plants, causing an incidental effect on the interstate price of capacity. Rather, LCAPP sets a price of capacity that will lead to the construction of new power plants. New Jersey cannot excuse LCAPP's interference with capacity prices as incidental to its scheme because the statute's explicit objective is to supplement capacity prices.

Nor can the statute be saved by the fact that its design incorporates, rather than repudiates, PJM's capacity auction clearing price. Recall that PJM pays generators for the capacity they supply to PJM, and it charges load-serving entities for the proportional share of the capacity they obtain though PJM. LCAPP supplements what the generators receive from PJM with an additional payment financed by payments from electric distribution companies, the public utilities that own local transmission lines. Because electricity distribution companies do not participate in PJM's capacity auction, and because PJM still pays generators the auction clearing price, LCAPP artfully steps around the capacity transactions facilitated by PJM. The arrangement does not save the law. "[I]f FERC has jurisdiction over a subject, the States cannot have jurisdiction over the same subject." *See Miss. Power & Light Co. v Miss. ex rel. Moore*, 487 U.S. 354, 377 (1988) (Scalia, J., concurring). Thus, we agree with the Fourth Circuit that "[t]he fact that [these sorts of payments] do[] not formally upset the terms of a federal transaction is no defense, since the functional results are precisely the same." *Nazarian*, 753 F.3d at

477. The generators receive a different price for the capacity they clear through PJM than what FERC intended.

IV. The Federal Field has Limits

Counsel to various state amici describe the District Court's preemption decision as unprecedented:

> This is the first time we have a state law to address state long-term energy needs under a state procurement paid for by state rate payers, [that] is nonetheless deemed to be field preempted under the Federal Power Act as well as conflict preempted because it might have an effect on the market when anything a state does for generation will have [an] effect.

Tr. of Oral Argument at 32:02-09 (March 27, 2014). In particular, LCAPP's defenders fret that a decision in favor of preemption will hamstring state-led efforts to develop renewable and reliable electric energy resources.

However broadly we might have decided this case, our holding today focuses instead on the field of interstate rates and, in particular, on capacity prices. Because we agree with the District Court that LCAPP and the Standard Offer Capacity Agreements attempt to regulate an exclusively federal field, we do not decide whether the District Court also correctly determined that LCAPP "poses as an obstacle" to PJM's markets and has been conflict preempted. *See* App'x 86. Thus, we have no occasion to conclude that PJM's markets preempt any state act that might intersect a market rule.

Nor do we endorse the argument that LCAPP has been field preempted because it affects the market clearing price by increasing the supply of electric capacity. *Cf.* FERC & United States Amicus Br. 11-17. Holding all else constant, an increase in capacity resources will cause supply to satisfy demand at a lower price. So LCAPP has the theoretical ability to influence the wholesale price of energy and capacity in PJM by enlarging the supply of capacity. If any effect on interstate markets could trigger preemption, LCAPP would be irredeemably flawed.

But the law of supply-and-demand is not the law of preemption. When a state regulates within its sphere of authority, the regulation's incidental effect on interstate commerce does not render the regulation invalid. *Nw. Cent. Pipeline Corp.*, 489 U.S. at 514. Accordingly, we do not view LCAPP's incidental effects on the interstate wholesale price of electric capacity as the basis of its preemption problem. Indeed, were we to determine otherwise, the states might be left with no authority whatsoever to regulate power plants because every conceivable regulation would have some effect on operating costs or available supply. That is not the law. The states may select the type of generation to be built—wind or solar, gas or coal—and where to build the facility. Or states may elect to build no electric generation facilities at all. *See Conn. Dep't of Pub. Util. Control v. F.E.R.C.*, 569 F.3d 477, 481 (D.C. Cir. 2009). The states' regulatory choices accumulate into the available supply transacted through the interstate market. The Federal Power Act grants FERC exclusive control over whether interstate rates are "just and reasonable," but FERC's authority over interstate rates does not carry with it exclusive control over any and every force that influences interstate

rates. Unless and until Congress determines otherwise, the states maintain a regulatory role in the nation's electric energy markets. Today's decision does not diminish that important responsibility.

V. Conclusion

We affirm the District Court's judgment. LCAPP compels participants in a federally-regulated marketplace to transact capacity at prices other than the price fixed by the marketplace. By legislating capacity prices, New Jersey has intruded into an area reserved exclusively for the federal government. Accordingly, federal statutory and regulatory law preempts and, thereby, invalidates LCAPP and the Standard Offer Capacity Agreements.

In deciding that LCAPP has been field preempted because it sets capacity rates, we do not accept the argument that field preemption will occur whenever a state's legislation indirectly affects matters within FERC's jurisdiction. By statute and tradition, states have a role to play in energy markets.

**APPENDIX B**

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

[Filed September 11, 2014]

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No. 13-4330

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PPL ENERGYPLUS, LLC; PPL BRUNNER ISLAND, LLC; PPL HOLTWOOD, LLC; PPL MARTINS CREEK, LLC; PPL MONTOUR, LLC; PPL SUSQUEHANNA, LLC; LOWER MOUNT BETHEL ENERGY, LLC; PPL NEW JERSEY SOLAR, LLC; PPL NEW JERSEY BIOGAS, LLC; PPL RENEWABLE ENERGY, LLC; CALPINE ENERGY SERVICES L.P.; CALPINE MID-ATLANTIC GENERATION, LLC; CALPINE NEW JERSEY GENERATION, LLC; CALPINE BETHLEHEM, LLC; CALPINE MID-MERIT, LLC; CALPINE VINELAND SOLAR, LLC; CALPINE MID-ATLANTIC MARKETING, LLC; CALPINE NEWARK, LLC; EXELON GENERATION COMPANY, LLC; GENON ENERGY, INC.; NAEA OCEAN PEAKING POWER, LLC; PSEG POWER LLC; ATLANTIC CITY ELECTRIC COMPANY; PUBLIC SERVICE ELECTRIC & GAS COMPANY

v.

LEE A. SOLOMON, in his official capacity as President of the New Jersey Board of Public Utilities; JEANNE M. FOX, in her official capacity as Commissioner of the New Jersey Board of Public Utilities; JOSEPH L. FIORDALISO, in his official capacity as Commission of the New Jersey Board of Public Utilities; NICHOLAS V. ASSELTA, in his official capacity as Commissioner of the New Jersey Board of Public Utilities;

CPV POWER Development, Inc.;

*Appellant*

*HESS NEWARK, LLC, Intervenor in USCA

*(Pursuant to Courts order entered November 14, 2013)

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No. 13-4501

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PPL ENERGYPLUS, LLC; PPL BRUNNER ISLAND, LLC; PPL HOLTWOOD, LLC; PPL MARTINS CREEK, LLC; PPL MONTOUR, LLC; PPL SUSQUEHANNA, LLC; LOWER MOUNT BETHEL ENERGY, LLC; PPL NEW JERSEY SOLAR, LLC; PPL NEW JERSEY BIOGAS, LLC; PPL RENEWABLE ENERGY, LLC; CALPINE ENERGY SERVICES L.P.; CALPINE MID-ATLANTIC GENERATION, LLC; CALPINE NEW JERSEY GENERATION, LLC; CALPINE BETHLEHEM, LLC; CALPINE MID-MERIT, LLC; CALPINE VINELAND SOLAR, LLC; CALPINE MID-ATLANTIC MARKETING, LLC; CALPINE NEWARK, LLC; EXELON GENERATION COMPANY, LLC; GENON ENERGY, INC.; NAEA OCEAN PEAKING POWER, LLC; PSEG POWER LLC; ATLANTIC CITY ELECTRIC COMPANY; PUBLIC SERVICE ELECTRIC & GAS COMPANY

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CPV POWER DEVELOPMENT INC.; HESS NEWARK, LLC.

LEE A. SOLOMON,
JEANNE M. FOX,
JOSEPH FIORDALISO,
NICHOLAS ASSELTA,

*Appellants*

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On Appeal from the United States District Court
for the District of New Jersey

(D.C. No. 3-11-cv-00745)

District Judge: Honorable Peter G. Sheridan

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Argued: Marsh 27, 2014

Before: FUENTES and SHWARTZ, *Circuit Judges*,
and ROSENTHAL, *District Judge*.*

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JUDGMENT

This cause came to be heard on the record from the United States District Court for the District of New Jersey and was argued on March 27, 2014. On consideration whereof, it is now hereby

ORDERED and ADJUDGED by this Court that the Order of the District Court entered on October 25, 2013 be and the same are hereby AFFIRMED. Costs taxed against the Appellants. All of the above in accordance with the opinion of this Court.

ATTEST:

/s/ Marcia M. Waldron
Clerk

Dated: September 11, 2014

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* Honorable Lee H. Rosenthal, U.S. District Judge for the Southern District of Texas, sitting by designation.

**APPENDIX C**

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

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Civil Action No.: 11-745

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PPL ENERGYPLUS, LLC, *et al*.,

*Plaintiffs*,

v.

ROBERT M. HANNA, in his official capacity as President of the New Jersey Board of Public Utilities, *et al*.,

*Defendants*.

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MEMORANDUM

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SHERIDAN, U.S.D.J.

This non-jury case was tried before the Court over thirteen separate days in April and May, 2013. After trial, the parties submitted proposed findings of fact and conclusions of law as well as briefs, and thereafter, summations were heard. The Court, having considered the parties' submissions and having deliberated over the facts and the law, submits this memorandum as its decision.

In broad terms, the issue before the Court is whether the New Jersey Long-Term Capacity Pilot Project Act, P.L. 2001, c. 9, approved Jan. 28, 2011, codified at N.J.S.A. §§ 48:3¬51, 48:3-98.2-.4 ("LCAPP"

or "Act"), should be declared unconstitutional as violating the Supremacy Clause, and whether the New Jersey Board of Public Utilities ("NJBPU", "BPU", or as referred to herein as the "Board") should be enjoined from engaging in activities in furtherance of the Act because the LCAPP is preempted by the Federal Power Act, 16 U.S.C. § 824 *et seq*. That is, whether actions by the State of New Jersey taken pursuant to the LCAPP intrude upon and interfere with the authority delegated to the Federal Energy Regulatory Commission (as referred to herein, "FERC" or "Commission") by the Federal Power Act.

Before proceeding to the substance of this case, the Court provides two cautionary observations regarding writing style and organization and a general reservation as to the presentation and scope of the findings within this decision. First, on writing style. The electric energy industry has its own jargon which makes great use of acronyms. With so many acronyms being used, the testimony and briefs become like alphabet soup where all the letters swirl around and may confuse the reader. As such, a list of acronyms which have been substantially agreed upon by the parties is attached as Rider A. The Court minimizes use of these acronyms in this decision. By way of reservation, the first part of the trial reviewed the extensive history of how the electric energy industry has developed into its present state. This opinion includes an overview of the relevant background for the purpose of providing sufficient information to decide the issues, however, it does not purport to be a historical work. And lastly on organization, there are many non-controversial facts presented within the Court's overview of the relevant background, and a new term may present itself without prior introduction. In this case, the term will be explained

later in the Court's decision. After sifting through a confluence of facts, the Court has gleaned a set of manageable facts with which to evaluate the preemption issue. The decision is subdivided into several sections: (A) an identification of the parties to the action; (B) an identification of important non-parties; (C) an identification of witnesses who testified at trial; (D) a description of some basic facts regarding electricity; (E) background information on the electric energy industry; (F) a description of the "Reliability Price Model" ("RPM") process; (G) a description of the LCAPP statute; (H) an explanation of the impacts of the LCAPP; (I) a description of the credibility of witness; (J) analysis; and (K) a conclusion.

## A. PARTIES TO THE ACTION

### 1. Defendants

New Jersey Board of Public Utilities. The defendants are Robert M. Hanna,[1] Jeanne M. Fox, Joseph L. Fiordaliso, and Nicholas Asselta, all of whom are current or former commissioners of the New Jersey Board of Public Utilities.[2] Each is named in his official

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[1] Mr. Hanna was named as President of the Board on December 21, 2011. At the time of the underlying facts, Lee A. Solomon served as Board President.

[2] In New Jersey, the Board has always been a distinguished public entity known for its practical and professional decision making. Over the years, many prominent New Jersey leaders have served on the Board. For example, Mr. Solomon and Mr. Asselta served in the New Jersey State Assembly. Both Governor Byrne and Governor Whitman have served as Board President. Moreover, William Hyland, a former New Jersey Attorney General who has served the State of New Jersey in many esteemed capacities, was a former Board President. In reviewing this matter, the Court has considered the Board and its members,

capacity against whom declaratory and injunctive relief is sought. Since each currently serves or formerly served as a commissioner on the Board, this opinion collectively refers to them as the "Board." The Board has broad statutory authority over the activities of public utilities within the State of New Jersey. *See In re Centex Homes, LLC*, 411 N.J. Super. 244, 254 (App. Div. 2009). Specifically, Title 48 of the New Jersey Statutes provides that the Board has "general supervision and regulation of and jurisdiction and control over all public utilities." N.J.S.A. § 48:2-13(a). As part of that authority, the BPU is authorized to require any public utility operating within the State to furnish safe, adequate, and proper service to consumer ratepayers at "just and reasonable" rates. N.J.S.A. § 48:2-21.

CPV Power Development, Inc. CPV Power Development, Inc. ("CPV") is an Intervenor/Defendant. CPV is a Delaware corporation that, through its subsidiaries, is engaged in the development, ownership, and management of natural gas-fired facilities in North America (T. 1587, 10-24). CPV owns and manages a natural gas-fired generation facility in Riverside County, California, and has taken steps to develop other natural gas-fired facilities, including projects in Maryland, New York and New Jersey. CPV began to develop its Shore Project in New Jersey prior to implementation of the LCAPP Act. (T. 1588, 6 through T. 1589, 17). Most importantly for purposes of this case, CPV was named an eligible generator under the LCAPP by the Board and cleared the RPM Auction on its 2012 bid (T. 1588, 15-22).

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their sound judgment, and their professionalism in furtherance of the public good.

2. Plaintiffs

The Plaintiffs are a group of wholesale, retail, and marketing companies who produce and sell energy and are located within the PJM market.[3] Several Plaintiffs are identified below.

Plaintiff Calpine Corporation is an electric generation and marketing corporation with a number of subsidiaries. It is a publicly traded, independent power producer based in Houston, Texas which operates ninety-one (91) power plants throughout the United States and Canada. The Calpine generation companies are physically located in the PJM market and participate in the PJM wholesale energy and capacity markets.

Plaintiff Exelon Generation Company, LLC is a Pennsylvania corporation headquartered in Kennett Square, Pennsylvania. Exelon Generation is a wholly-owned subsidiary of Exelon Corporation. Exelon Generation's business consists of owning and operating electric generating facilities, wholesale power marketing operations, and competitive retail supply operations. Exelon Generation sells energy and capacity in the PJM interstate market and competes in PJM's wholesale capacity auctions.

The PPL Parties are a group of related companies principally located in Allentown, Pennsylvania which are market and generation subsidiaries of PPL Corporation. They are physically located in the PJM market and participate in the PJM wholesale energy and capacity markets. Together they control or own

[3] Plaintiffs GenOnEnergy, NAEO Ocean Peaking Power, and Essential Power were never substantively discussed during trial and no injury was presented.

about 19,000 megawatts of generating capacity in the United States, some of which is located within the PJM market.

Plaintiff PSEG Power, LLC is a Delaware limited liability company, headquartered in Newark, New Jersey. PSEG Power is a wholly-owned subsidiary of Public Service Enterprise Group, Inc.. PSEG Power owns approximately 11,850 megawatts of generating capacity within the PJM area, approximately 9,950 megawatts of which is located in New Jersey. PSEG Power sells energy and capacity at wholesale in interstate commerce, including in PJM's capacity and energy markets.

Plaintiff Public Service Electric and Gas Company ("PSE&G"), a subsidiary of Public Service Enterprise Group, is located in New Jersey and is one of the largest combined electric and gas companies in the United States. It is also New Jersey's oldest and largest publicly owned utility. PSE&G currently serves nearly three quarters of New Jersey's population from Bergen to Gloucester Counties.

Plaintiff Atlantic City Electric Company, based in New Jersey, is a subsidiary of Pepco Holdings, Inc., which provides electric service to approximately 547,000 customers in southern New Jersey. Pepco Holdings, Inc. is one of the largest energy delivery companies in the Mid-Atlantic region, serving about 1.9 million customers in Delaware, the District of Columbia, Maryland and New Jersey.

B. OTHER IMPORTANT NON-PARTIES

The Federal Energy Regulatory Commission ("Commission" or "FERC") and PJM Interconnection, LLC ("PJM") are two entities that are key players in the sale and delivery of energy. The Commission and

PJM are not parties to this action, but are discussed throughout this memorandum.

Pursuant to the Federal Power Act, 16 U.S.C. § 824 *et seq*., the Commission has federal statutory authority to regulate the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce. (Stipulated Facts ¶ 5). In this case, the scope of the Commission's jurisdiction in regulating the sale of electric capacity in the wholesale market, and whether such jurisdiction is exclusive or concurrent with the Board's jurisdiction, is at issue. The applicable federal statute from which the Commission derives its authority reads:

> (b) Use or sale of electric energy in interstate commerce.
>
> (1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of

> electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter. 16 U.S.C. § 824(b)(1).

PJM Interconnection, LLC is a voluntary association of different energy stakeholders which includes administrative bodies and electric generators.[4] (Stipulated Facts ¶ 13). PJM is primarily subject to Commission regulation through a tariff. It operates a regional wholesale market that includes all or part of thirteen states including New Jersey. In addition, PJM is a regional transmission organization ("RTO"). (T. 47, 17 through T. 48, 11).

PJM was originally founded in 1927. The name "PJM" is the brainchild of its earliest members who were from the states of "Pennsylvania (P), New Jersey (J), Maryland (M)". (T. 410, 22 through T. 411, 8). It was formed as a "power pool" for traditional utilities which recognized that a regional transmission organization could easily accommodate sharing of electric capacity more efficiently (T. 39, 5-10). The sharing of electrical capacity through such arrangements drastically drops consumer costs by limiting the number of electrical generation facilities required for peak hour production. As noted above, PJM operates pursuant to a tariff filed by PJM with the Commission

[4] PJM was not well defined at trial. The issue of how these competing companies and regulatory bodies interact in terms of governance and voting procedures was not adequately addressed by any of the litigants.

called the "Open Access Transmission Tariff" (Stipulated Facts ¶ 23).

PJM has been a relatively successful operation. For instance, today, PJM is the "largest centrally dispatched power market . . . in the world," covering 60 million customers and 185,000 megawatts. (T. 69, 20 through T. 70, 1). Within PJM there are over 1,300 power plants and approximately 56,000 miles of transmission lines. (T. 406, 24 through T. 407, 11). Mr. Massey testified that PJM is the most sophisticated of all of the regional transmission organizations. In fact, "there are government officials and market participants from around the world that regularly travel to PJM for briefings about how the markets work. So [it is] considered state of the art." (T. 70, 1-8).

Gradually, the traditional utilities within PJM transferred operational control of all their transmission to PJM. Currently, PJM is responsible for "[m]anaging a regional transmission grid encompassing all or part of thirteen states and the District of Columbia." (Stipulated Facts ¶ 11).

PJM, under the supervision of the Commission, is "responsible for planning the electric system to preserve the reliability of the electricity supply" in New Jersey. (Pl.'s Ex. 45, at 27). That is, PJM "plan[s] expansions to transmission to improve the ability to transmit energy from where it is generated to serve load." (Stipulated Facts ¶ 11). Most importantly, PJM is also responsible for the "dispatching" of generation in real time. It does this from "a very sophisticated control room in Valley Forge, Pennsylvania . . . which looks like an air traffic control system." (T. 50, 6-13). From this control room, PJM "direct[s] this generator[], to ramp up [and] . . . to ramp down all in real time. Because over this 13 state area they must insure

that supply and demand are matched almost perfectly in real time." (T. 50, 12-13). Despite these functions, PJM has no authority to construct or build a power plant, and likewise it has no authority to retire antiquated power plants. (Def.'s Ex. 183).

C. TESTIFYING WITNESSES

There were a number of witnesses who testified at trial, each of whom is identified below. All of these witnesses were very professional and proficient in their careers, and the Court weighed their credibility in light of these qualifications.

1. Plaintiffs' Witnesses

William L. Massey obtained his Law Degree from the University of Arkansas School of Law in 1973, and later earned an LLM from Georgetown University Law Center in 1985. Upon his law school graduation, he clerked for the U.S. Circuit Court of Appeals for the Eighth Circuit. He later became Chief Counsel for U.S. Senator Dale Bumpers of Arkansas, where he focused on energy matters before the Senate Committee on Energy and Natural Resources. President Clinton later appointed Mr. Massey to be a Commissioner of the Commission where he served for over ten years. Mr. Massey currently serves as a partner in the Washington, DC office of the law firm Covington and Burling and is an Adjunct Professor at the Georgetown University Law Center. Mr. Massey was qualified as an expert "in the history and evolution of the electricity industry." (T. 23, 12-15).

Joseph Dominguez is the Senior Vice-President for Governmental and Regulatory Affairs and Public Policy for Exelon Corporation. He obtained a Bachelor of Science Degree in Mechanical Engineering from the New Jersey Institute of Technology and a Law Degree

from Rutgers University School of Law. He previously worked at the law firm of White & Williams in Philadelphia, Pennsylvania and served as an Assistant United States Attorney in the Eastern District of Pennsylvania.

Robert D. Willig, Ph.D. is a Professor of Economics and Public Affairs at Princeton University. Professor Willig studied mathematics at Harvard College and later obtained a Masters of Arts in Operations Research and Statistics, and a Doctorate in Economics from Stanford University. Professor Willig previously worked at Bell Labs performing research on the theory of economic regulation of regulated industries. After working there for five years, he became a Professor of Economics and Public Affairs at Princeton in 1978. Professor Willig's specialty is industrial organization which involves the interrelationships between business, technology, the marketplace, and government. He was qualified as an expert in the fields of economics and regulatory policy with particular expertise in electric energy. (T. 623, 21-25).

Michael Cudwadie is employed by PPL Energy Plus as Vice-President of Trading East. In that role, he is responsible for the hedging and trading activities of 9,000 megawatts of generation in the PJM markets. He has a Bachelor's Degree in Accounting from Pennsylvania State University, and an MBA from Lehigh University.

Zamir Rauf has been employed by Calpine Corporation as its Chief Financial Officer since 2008. In that role, he is responsible for the accounting and treasury functions of Calpine which include project finance, investor relations and risk management.

Daniel Cregg is the Vice-President of Finance for PSEG Power within PSEG Services Corporation. In this role, he develops business plans and near term earnings forecasts, prepares forecasts of market direction and analyzes elements of major investment decisions. He has a Bachelor's Degree in Accounting from Lehigh University and an MBA from the University of Pennsylvania's Wharton School of Business.

Anthony Robinson is employed by PSE&G as Director of Basic Generation Service and Basic Gas Supply Service. He has a Bachelor's Degree in Economics, Applied Math and Statistics from Stoney Brook University. (T. 939, 14-17).

2. Defendants' Witnesses

James P. Giuliano is Director of the New Jersey Board of Public Utilities' Division of Reliability and Security. He is responsible for natural gas pipeline safety, underground damage prevention and emergency management and security. He has a Bachelor's Degree in Communications, and has completed many state certifications in courses related to his job.

Oden Sherman Knight is the Senior Vice President of Marketing and Organization at CPV where he manages power sales and gas purchases. (T. 1584, 16). He has a Bachelor's Degree in Mechanical Engineering from Stanford University and a Masters in Business from Columbia University (T. 1584, 4-7).

Craig R. Roach is a principal of Boston Pacific Company, a consulting firm which focuses on power plant development. He has a Bachelor's Degree in Economics from John Carroll University and a Doctorate in Economics from the University of Wisconsin. Mr. Roach was qualified as an expert in the

design and implementation of competitive procurements and competitive markets for electricity.

Mr. Richard L. Levitan was the Board's advisor for implementation of the LCAPP. He has served as President of the consulting firm Levitan & Associates since its founding in 1989. The firm provides management consulting and analytic expertise to regional transmission organizations and short form independent system operators. He is a graduate of Cornell University and received a Masters with a specialization in Energy Economics from Harvard University.

D. BASIC FACTS REGARDING ELECTRICITY

Energy is "the actual electricity" that electric generators produce and which residential and business consumers ultimately use.[5] (Stipulated Facts ¶ 20). It cannot be stored in quantities large enough to supply customers during times of peak demand. (*Id*.). That is, energy cannot be canned or placed in a battery for a long period of time. It has no shelf life. As a result, "energy generally must be produced when it is needed, and at the rate at which it is consumed." (Id.) As Mr. Massey stated during his testimony, "[o]ne of the things about electricity is that it cannot be easily stored, and so supply and demand have to be matched instantaneously in real time." (T. 35, 4-6).

Energy is a product in interstate commerce. Regardless of which generator dispenses the energy, it ordinarily travels through interstate commerce to reach its destination. In 1927, the Supreme Court held that the interstate commerce clause prohibits states

[5] Residential and business customers are often referred to as "consumers" or "ratepayers."

from regulating the rates for wholesale energy sales between utilities in different states because those sales are interstate transactions. *Pub. Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927); (Stipulated Facts ¶ 4). Surprisingly, no witness precisely described the logistics of an energy delivery transaction (*i.e.*, how energy is transmitted from a generator to a consumer) except to say that the delivery of energy is overseen by PJM and PJM routes energy through its transmission system. (T. 50, 6-13)

Amount of Energy. Energy is usually measured in megawatts. One megawatt of electricity powers approximately 1,000 households. Usually, megawatts are associated with lengths of time such as "per day" or "per hour." (Stipulated Facts ¶ 18).

Capacity. "Capacity" is defined as "the ability to produce electricity when called upon." (Stipulated Facts ¶ 17). In essence, capacity is the ability to produce sufficient energy to meet demand. At certain times, such as during the summer months when temperatures increase, demand for energy increases. Regardless of fluctuations, there must be sufficient capacity to meet the demand of high energy use at all times.

Capacity Resources. "Capacity resources include electric generation facilities (*e.g.*, nuclear, natural gas, coal, wind, or solar), demand resources (*i.e.*, the ability to call upon consumers to reduce their electricity demand), and energy efficiency resources (measures that reduce demand)." (Stipulated Facts ¶ 19).

Reliability. "Reliability" is the delivery of electricity to customers in the amounts desired and within acceptable standards for frequency, duration and magnitude of outages and other adverse conditions or

events. (T. 81, 23 through T. 83, 12). According to Mr. Levitan, electric reliability means being able to "keep consumers' lights on" under duress and maintaining the power system when operating contingencies arise. (T. 1549, 8-11); see also I/M/O the Petition of Public Service Gas and Electric Company for a Determination Pursuant to the Provisions of N.J.S.A. 40:55D-19 (Susquehanna-Roseland Transmission Line). Resource adequacy is a key component of reliability. (T. 1549, 6-14). The key factor in meeting the reliability standard is having sufficient generators and transmission lines available to deliver energy as required by the circumstances.

Generation Plants. Generation plants are categorized into three types—base load, mid-merit, and peaking plants. The parties agree on the definition of base load and mid-merit. A base load plant is a plant that operates all or most of the time. A mid-merit plant, such as a combined-cycle gas turbine, is a plant that operates less than a base load plant but more than a peaking plant. The parties disagree on the definition of a peaking plant; but generally, a peaking plant is "a gas turbine, a simple cycle unit, a unit that is typically run sparingly, a unit that has certain technology characteristics that allow it to get started from a cold stand-by mode, and achieve full operation in just a few minutes." (T. 1289, 12-16).

## E. BACKGROUND OF THE ELECTRIC ENERGY INDUSTRY

In the beginning of the twentieth century, the New Jersey Legislature, like many other state legislatures at the time, enacted a statute creating a public utility to oversee the operation of electric and gas utilities. During the early stages of utility regulation, states had exclusive authority over such utilities. During this

time, the energy industry "was dominated by vertically integrated utility companies" (hereinafter, referred to as "traditional utilities")[6]. (T. 24, 24 through T. 25, 1); (Stipulated Facts ¶ 1).

Typically, the traditional utility was granted an exclusive right by state and local governments to provide electric service to all consumers located in a defined territory. The traditional utility also had other powers, such as eminent domain authority, that would allow it to construct and operate power plants and local distribution networks to connect those power plants to local customers. In return, the traditional utility obligated itself to operate as a "common carrier" with the duty to provide service on a non-discriminatory basis, and to subject its rates to regulation by a state public utility commission. The regulatory standards adopted by state commissions permitted rates that would reimburse utilities for their costs incurred in providing service and debt incurred in financing the construction of power plants and other equipment. The standards were also meant to afford investors in these utilities a reasonable rate of return. This structure enabled the traditional utility to raise capital through the issuance of stock or selling of debt, which, in turn, would allow the utility to expand its facilities. Recovery of and on an investment in a traditional utility, however, was always subject to a "prudence review" by the Board in New Jersey. (Stipulated Facts ¶ 2).

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[6] The parties refer to the traditional utility as a "vertically integrated utility." For purposes of minimizing confusion, this memorandum uses the term "traditional utility" because the word "utility" is now associated with an electric distribution company (EDC).

In 1927, the Supreme Court of the United States decided the landmark case *Pub. Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927). In that case, the Public Utilities Commission of Rhode Island attempted to regulate the sale of electricity from the Narragansett Electric Lighting Company to the Attleboro Steam & Electric Company located in Massachusetts. The Court struck down the Public Utilities Commission of Rhode Island's efforts deeming that its regulation had placed a direct burden on interstate commerce. The Court's decision ultimately created a regulatory gap wherein no regulator had the authority to oversee interstate transactions made by traditional utilities.

In 1935, envisioning that the federal government should have a role in regulating interstate energy transactions, Congress enacted the Federal Power Act, which gave the Commission exclusive regulatory authority over "the transmission of electric energy in interstate commerce" and "the sale of electric energy at wholesale in interstate commerce. 16 U.S.C. § 824(b). While the statute vested this authority in the Commission, it also "reserved to the States certain . . . regulatory authority, including that over generation facilities." (Stipulated Facts ¶ 5). Under the statute, state commissions "continued to regulate local utilities' construction of new power plants, operations, and rates charged for retail service to customers" including "the costs incurred by local utilities in constructing and operating the power plants they used to generate electricity to service their retail customers. (*Id.*) From 1920 until the late 1980s, utilities operated under the concurrent supervision of both federal and state regulations. During that time, the Board and Commission acted cooperatively and respected their jurisdictional limits.

Before the advent of federal authority in the electric power industry, a traditional utility "performed three main operational tasks: it built, owned, and operated electric power plants; it transmitted electricity from the power plants to the area of service in which it enjoyed a monopoly; and it distributed the electricity to its customers in that area of service using its local distribution network, that is, the poles and wires that it owned and maintained." (Stipulated Facts ¶ 1). Each traditional utility was, in essence, a "single company" that "generated power, transmitted that power, and distributed that power to its own customers, the homes and businesses that it serves". (T. 2008, 13-18). In these early years, there was little to no relationship among the traditional utility companies, so each company generally only produced sufficient capacity to service its own customers' needs. Each traditional utility had a service territory established by state regulation, a monopoly for electricity service within that territory, and an obligation to serve all customers in that service territory. "[I]n return for fulfilling that obligation to serve all customers, [traditional utilities] were given an assurance of a reasonable rate of return." (T. 27, 16-21); (Stipulated Facts ¶ 2). As a result, a traditional utility's sales of electricity to residential and business users within its service territory were considered retail sales to consumers and "largely regulated at the state level." (T. 25, 5-6); (T. 30, 12-13); (Stipulated Facts ¶ 5).

Often the lack of interaction among traditional utilities created inefficiencies because each utility would construct its own power plants to meet peak electric demand; that is, each traditional utility "was insuring that it had enough capacity to serve its own load." (T. 37, 16-18). Because electricity demand peaks at limited times throughout the year, a utility may

have needed to build a power plant that runs only "10, 15, 20, 50 hours a year." (T. 35, 3-13). As a result, each traditional utility tended to have "plants that [were] sitting idle most of the time, because they [were] needed for a few hours." (T. 37, 16-24). "[T]hat created some inefficiencies in the sense [that] . . . too many power plants to provide this capability were being built." (T. 37, 16-24).

In the early twentieth century, some electric utilities smartened up, adjusted their strategy, and "began to sell power or standby capacity to each other." (Stipulated Facts ¶ 3). In order to accomplish this, the traditional utilities "built high voltage transmission lines among them in order to transact such 'wholesale' purchases and sales. This allowed utilities to lower costs because they no longer had to maintain sufficient capacity to supply peak demand at all times; instead, they could contract bilaterally in the interstate wholesale market to ensure that they had access to sufficient resources to supply peak demand when it was needed." (Stipulated Facts ¶ 3). Thereafter, to protect against outages, traditional utilities would buy and sell capacity from one another for future years, so that they could be assured they would have sufficient supply when operating contingencies arose, without having to develop more power plants.

As the traditional utilities engaged in increased wholesale sales and capacity purchases, the need for federal regulation became more obvious. In order to manage stand-by capacity sales, PJM was created to ensure reliability by managing interstate transmission lines and, in more recent years, by designing and operating wholesale auctions.

Deregulation of Wholesale Energy Sales by the Commission

In the 1980s, when governmental deregulation of business entities was a prevalent feature of federal policymaking, some federal legislators brainstormed that the structure for sales of energy and energy capacity could be modified from one in which sales were made at a governmentally imposed rate to one that was more economically efficient, competitive and based on the economic theory of supply and demand. This idea ultimately culminated in several initiatives during the 1990s.

In 1992, Congress enacted the Energy Policy Act of 1992 ("EPAct"), Pub. L. No. 102¬486, 106 Stat. 2776, which authorized the Commission to ease restrictions on access to interstate transmission wires. This allowed more electric generators to provide energy to a broader area, and recognized the concept of separating generation facilities from other parts of traditional utilities. That is, the generation segment of a traditional utility could operate separately from the other segments of the utility. A key objective of the Energy Policy Act was to "encourage[e] the development of independent generators" — sometimes referred to as "independent power producers" — "that could sell into the marketplace." (T. 44, 11 through T. 46, 25).

In 1996, the Commission issued Order Number 888 which required "transmission owners in the United States . . . to offer access to their transmission wires to third-parties . . . on a non-discriminatory basis." (T. 45, 12-19). "Order 888 opened the transmission grid, and competition began to develop, and . . . . wholesale markets were actually emerging regionally." (T. 47, 12-16). In 1996, through Orders 888 and 889, the

Commission "established national open-access rules that required all transmission-owning utilities under its jurisdiction—*i.e.*, those utilities that 'own, control, or operate transmission facilities used for transmitting electric energy in interstate transmission'—to provide non-discriminatory transmission access under standardized tariffs. One significant impact of Orders 888 and 889 was to increase the opportunity for non-utility generators to sell their power to additional markets." (Stipulated Facts ¶ 8).

In December 1999, the Commission issued Order 2000 which encouraged industry participants to organize themselves into large regional entities called regional transmission organizations ("RTO"). The creation of such organizations "allow[ed] for regional operation of the transmission system and provide[d], among other things, a platform for regional wholesale electricity markets." (Stipulated Facts ¶ 9). Notably, PJM is an RTO.

PJM adapted some of its functions to meet the requirements of these statutes and regulatory directives. Most importantly, PJM instituted three types of wholesale markets: "[the] capacity market, the energy markets and the ancillary services markets." (T. 74, 21 through T. 75, 23). Each of these markets has a special function:

(a) the "regional capacity market, called the reliability pricing model (RPM), annually sets the price of capacity" three years forward. The controversy in this case involves the regional capacity market. (T. 74, 23-24).

(b) the energy markets price the cost of energy produced by the generators and used by consumers. (Stipulated Facts ¶ 20). PJM operates a "day ahead"

energy market, meaning "generators offer to supply power into the market a day ahead of real time." The day ahead market is a "planning tool that PJM uses to [e]nsure that it knows a day ahead of time what resources are going to be available 24 hours thereafter, when the generation is actually dispatched to keep the lights on." PJM also operates a "real time energy market, which is an hourly market that is close to the time of operation. And capacity resources bid into that market, and offer to supply . . . the actual electricity." (T. 74, 21 through T. 75, 23); and

(c) the ancillary services markets price the sale of "ancillary services" such as "spinning reserves and load-following services" to improve reliability. (T. 74, 21 through T. 75, 23).

Deregulation of Electric Generators by the Board

Following the federal lead, many traditional utilities chose to restructure by separating their generation functions from their transmission and distribution functions. (Stipulated Facts ¶ 6). According to Mr. Massey, there were two methods to accomplish this. First, the traditional utilities could sell or transfer their power plants to a competitive generation company. Second, the traditional utilities could "create an affiliate corporation . . . within a holding company to own the generation." (T. 53, 13-21). During the 1990s, many states restructured their electric industries to promote competitive markets in wholesale power generation. "Typically, the [s]tate-ordered restructuring resulted in the unbundling of [traditional] utilities into separate generation, transmission, and distribution companies. The distribution entities came to be known as 'Electric Distribution Companies' or 'EDCs[.]" (Stipulated Facts ¶ 6). In some cases, "restructuring also enabled

third parties with no distribution assets to compete in the sale of electricity at retail." (*Id*.) These entities are referred to as "Load Serving Entities" ("LSEs") (*Id*.).

In 1999, New Jersey followed suit. It restructured its utilities in a slightly different format than described above, but with the same result. In enacting the Electric Discount and Energy Competition Act ("NJ Energy Competition Act"), N.J.S.A. § 48:3-49 *et seq*., the New Jersey legislature unbundled the sale of energy to retail customers. The consumer could choose to be served by one of several load serving entities which would compete to provide service. These LSEs would deliver the energy through an electric distribution company ("EDC"). (T. 59, 2-9). As Mr. Dominguez explained in his testimony, the driving force behind the NJ Energy Competition Act was "customer choice"—that customers would have the right to choose their electricity suppliers or LSE. (*Id*.) Although the New Jersey Legislature focused on the benefit to the consumer, the NJ Energy Competition Act also "required the State's [traditional] electric utilities to divest themselves of electricity generation assets." (Stipulated Facts ¶ 7). Once the generation component was stripped, the word "utilities" became associated with the term "electric distribution companies" because EDCs were responsible for distributing electricity over local distribution networks to consumers in monopolistic service areas and were required to act as common carriers.[7] "The electricity itself was supplied by retail electric suppliers, that is, LSEs." (Stipulated Facts ¶¶ 7, 9).

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[7] The electric distribution company is referred to as a utility, but its operation is not as expansive as a traditional utility.

At the time of enactment, the New Jersey Legislature recognized the magnitude of this fundamental change by declaring that "this bill would effectively end the system of government regulation of the electricity generation industry, which has existed in New Jersey since the years when Woodrow Wilson served as Governor." Electric Discount and Energy Competition Act, P.L. 1999, c.23. eff. Jan. 25, 1999. Hence, the NJ Energy Competition Act recognized the demise of the traditional utility and the transformation of the electric energy industry into a more market driven system. Further, although the federal and state statutory amendments opened new competitive markets through restructuring, the State retained its authority over the siting and construction of power plants. (T. 167, 9 through T. 169, 6). So, after restructuring by the federal and New Jersey governments, the electric energy industry operates in the following manner:

(a) generators may sell energy and capacity at wholesale prices to PJM or negotiate power supply agreements (T. 64, 11 through T. 65, 4);

(b) PJM transmits and sells energy to load serving entities ("LSEs"); and

(c) LSEs sell to consumers and distribute the energy through electric distribution companies ("EDCs") which have monopolistic service areas and operate as common carriers. Since the EDC transmits the electric to consumers within its monopolistic area, it receives a delivery fee from the LSE.

In New Jersey, there are four EDCs: Rockland Electric Company, Public Service Electric & Gas Company ("PSE&G"), Jersey Central Power & Light Company ("JCP&L"), and Atlantic City Electric. (Pl.'s

Ex. 45, at 16-17). Each EDC owns and operates the local distribution wires located within its service territory. (T. 66, 17-22). After the restructuring, the State's utilities "became more commonly known as 'electric distribution companies' ('EDCs') because they were responsible for distributing electricity over local distribution networks." (Stipulated Facts ¶ 7). An EDC is sometimes referred to as the "local utility," but "the term EDC, electric distribution company, is intended to convey that this company is in the business of delivering electricity." (T. 56, 6-12). The electricity sold to retail customers by LSEs is delivered by the EDC within their local distribution networks.

The 2008 New Jersey Energy Master Plan authorized by the Board summarized the importance of the NJ Energy Competition Act:

> The owners of New Jersey power plants now have no legal expectation that they can recover all of their costs or a guaranteed return from retail customers. Hence, the plant owners (and their financiers) make their own decisions to invest in existing or new power plants, without [Board] oversight. They also make their own decisions about the price, using market signals, at which they are willing to sell their electricity, without traditional [Board] oversight. (Pl.'s Ex. 45, at 16).
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> PJM, under the supervision of [the Commission], is responsible for planning the electric transmission system to preserve the reliability of the electricity supply in its territory. Electric generation companies and

> their financiers make decisions about how much generating capacity will be built, what types of power plants will provide that new capacity, and where the new plants will be located; those companies also decide what plants will be kept in service and what plants will be retired. Those decisions are informed by economic signals from the wholesale electricity markets that PJM designs and administers, again under the supervision of the [Commission]. (*Id*. at 27).

Despite deregulation which provided generators with more decision making powers, the Commission and PJM do not have substantial authority to require construction of power plants, prevent retirement of generation, select the generation technologies that will be constructed, or require demand resource or energy efficiency programs as a means of addressing resource adequacy. (Def.'s Ex. 563). However, as previously noted, the restructuring of the traditional utilities required PJM and the Commission to institute three competitive markets which effect energy and capacity prices. The market of primary interest in this case is the regional capacity market called the reliability pricing model ("RPM").

F. THE RELIABILITY PRICING MODEL ("RPM")

The RPM is intended to "secure sufficient capacity resources to meet standards for serving the highest aggregate demand of the region's electric customers." (Stipulated Facts ¶ 12). To meet that objective, the RPM "establishes an annual Base Residual Auction (BRA') [or "RPM Auction"] through which PJM administers procurements of capacity." (*Id*.)

The RPM conducts the RPM Auction each May to secure the capacity that will be needed three years in the future. (T. 419, 3-8); (Stipulated Facts ¶ 25). New Jersey is a voluntary member of PJM and is a part of the RPM market. (Stipulated Facts ¶ 13). RPM is a provision of the PJM tariff which is approved by the Commission. (Stipulated Facts ¶ 23); (T. 80, 25 through T. 81, 4); (Def.'s Ex. 184). As the parties stipulated:

> Through the [RPM Auction] PJM seeks to procure . . . the amount of capacity that it has determined . . . will be needed to meet the system (or in some cases, the Locational Deliverability Area ('LDA')) peak three years in the future, plus a reserve margin. PJM then bills each participating load serving entity for its load-ratio share of the costs incurred by PJM to secure that capacity through the [RPM Auction]. (Stipulated Facts ¶ 26).

Generally, "The [RPM Auction] is a 'forward market,' meaning capacity is sold three years in advance of when it is needed. For example, the auction held in May 2012 [which is the subject of this lawsuit] concerned offers to sell capacity to be 'delivered' beginning June 1, 2015, through May 31, 2016." (Stipulated Facts ¶ 27).

RPM was designed to provide price signals for both new and existing generation. PJM Interconnection, LLC, 132 F.E.R.C. ¶ 61,173, 61,870 (2010). The Commission has emphasized that "RPM was designed to provide long-term forward price signals, and not necessarily long-term revenue assurance for "generators and developers." (Pl.'s Ex. 55, at 55-56). As Mr. Dominguez stated, "the RPM is a market-based

mechanism that uses economic price signals to indicate scarcity and need for capacity," and generators will decide from the price signal whether or not to expand or create new generation. (T. 413, 1-8).

"In the [RPM Auction] capacity resources . . . bid to supply capacity to PJM for one year beginning three years in the future, each offering to supply a particular quantity of capacity at an offer price." (Stipulated Facts ¶ 28). The bids of capacity resources are "stacked" from lowest-cost bids to highest-cost bids to construct a supply curve. (T. 92, 19-25). PJM also constructs a demand curve that is based on a forecast of peak electricity demand ("peak load"), plus a reserve margin. (T. 661, 13 through T. 662, 19). The PJM "reserve margin" is typically around 15 percent or more. The reserve margin addresses the possibility that "some plants might fail, might not be able to meet their obligation," or that there could be a "transmission outage." (T. 89, 25 through T. 90, 13). As Mr. Massey indicated, "[i]t also takes into account the fact that . . . [it is] hard to forecast electricity usage perfectly." (T. 90, 2-3). "And so this reserve margin is an insurance policy." (T. 90, 7). "The price of capacity in the [RPM Auction] is set by the intersection of supply and demand and is referred to as the 'clearing price.' That is, any capacity supplier that bids at or below the clearing price 'clears' the [RPM] auction and receives the clearing price for that capacity. Any capacity supplier that bids above the clearing price fails to 'clear' the [RPM] auction, and its capacity does not sell in the auction." (Stipulated Facts ¶ 29). The clearing prices for capacity sold in the RPM are the Commission approved rates for capacity sales made in PJM territory. (Pl.'s Ex. 26). When a generation resource has cleared the auction, it obligates itself to run through the delivery year. (T. 473, 22 through T.

474, 7). Thus, a capacity resource that clears the RPM Auction commits itself to make any investments necessary to fulfill its obligation. It also obligates itself to bid into the PJM energy and ancillary services markets. (T. 426, 1 through T. 473, 17).

As Mr. Dominguez testified, RPM is designed to procure the least expensive mix of resources that are necessary to keep the lights on for that one year period, three years hence. (T. 414, 14-18). Generally, the RPM Auction says to market participants "I am willing to serve capacity for one entire year three years forward." (T. 414, 14-18). "The purpose" of RPM was to "guarantee[] that the reliability target in PJM is met in the least cost possible way." (T. 763, 13-23). As PJM has explained to the Board, its "RPM Capacity Market is designed to commit the least-cost set of capacity resources to ensure that [Commission]-established resource adequacy targets are met in the PJM footprint on a three-year forward basis." (Pl.'s Ex. 230, at 10).

Generally, the single clearing price encourages capacity resources to operate more efficiently while keeping prices low. "[A] competitive market with a single, market-clearing price creates incentives for sellers to minimize their costs, because cost-reductions increase a seller's profits. And when many sellers work to minimize their costs, competition among them keeps prices as low as possible. . . . This market result benefits customers, because over time it results in an industry with more efficient sellers and lower prices." PJM Interconnection, LLC, 117 F.E.R.C. ¶ 61.331, 62678 (2006); (Pl.'s Ex. 19, at 57); (T. 436, 8-24). As Mr. Massey indicated, since there is a single price for the commodity, "the person who can provide the [capacity] cheapest will do the best in that market; [and the]

person who cannot provide the [capacity] competitively is either going to go out of business or figure out how to do better." (T. 436, 19-24). Mr. Massey explained "economists would say it's the law of one price. . . . It [does not] matter whether the electric energy's produced by an old generator [or] new generator, [it is] electric energy, it has the same value in the marketplace. And that [is] why pursuant to [Commission] rules that single clearing price model is used." (T. 92, 19 through T. 93, 23).

Despite the goal of reaching a highly competitive price through the RPM Auction, price varies in certain areas of the PJM market. For example, in New Jersey the price is higher than that in western Pennsylvania because the transmission costs associated with delivering the energy in New Jersey are more costly. (Def.'s Ex. 204). "For purposes of the RPM, PJM is divided into regions known as [Locational Deliverability Areas, or] LDAs." (Stipulated Facts ¶ 30). "New Jersey is located in a Locational Deliverability Area called 'EMAAC,' which also includes parts of Maryland, Pennsylvania, and Delaware. EMAAC is located within a wider [LDA] called 'MAAC,' which includes EMAAC, additional parts of Pennsylvania and Maryland, and the District of Columbia." (Stipulated Facts ¶ 31). According to the parties, within EMAAC, "there are smaller LDAs, including (within New Jersey), one called 'PSEG', and within the PSEG LDA, another one called 'PSEG North.'" (Stipulated Facts ¶ 33). As the parties explained:

> When constraints on the transmission lines limit the amount of electricity that can be imported into an LDA, RPM capacity prices can be higher in the constrained LDA—

> reflecting the fact that the LDA must rely on more expensive capacity resources located within the LDA rather than cheaper capacity resources located elsewhere. (Stipulated Facts ¶ 33).

Prices are often different among the LDAs leading to "price separation." As the Commission has explained, "[c]apacity market prices must be locational in order to be fully effective. Because of transmission constraints, capacity in one location is not always deliverable to loads in other locations[.]" (Pl.'s Ex. 26, at 34). As such, separate capacity prices are necessary to reflect the differences in costs and capacity needs among the locations. "Further, if a single capacity price is set for the entire region, capacity prices do not reflect the need for generation" in those particular locations. (*Id*.) For instance, as Mr. Dominguez stated "higher price for capacity gives a signal to those in the generation industry to consider developing a new plant or resource within the LDA because a better profit could be realized." (T. 445, 24 through T. 446, 12). "[T]his price differential is reflective of the transmission constraints in moving power from west to east into New Jersey and [signals] the need for resources to be located inside New Jersey." (Pl.'s Ex. 75, at 7).

From its initial inception in the early 2000s, the Board did not accept the RPM theory. Rather, the Board predicted that RPM would curtail development of new generation into New Jersey. The Board recommended that new generators should be given assurances to overcome fears regarding the risk of long term financing packages of potential financiers. The Board also complained that the RPM functions unfairly against new generators. First, the Board

argued that the long term price signals of the RPM Auction were insufficient to attract new generators in New Jersey since little development had occurred. (Pl.'s Ex. 197). Second, the Board argued that financial institutions were reluctant to loan money for development because of uncertainty. That is, capacity prices fluctuate and the clearing price of the RPM Auction only lasts a year ultimately rendering a long term loan very speculative. In reality, these variables caused energy prices to increase in New Jersey. As then-Board Commissioner Frederick Butler advised the Commission in February 2006:

> RPM, in its current form, will not have the intended effects on investment and will not result in the most cost effective means of solving future reliability problems. Thus, we are concerned that RPM, in its current form, will not ensure adequate electricity supply within New Jersey, and will lead to increased costs to our consumers. (Pl.'s Ex. 13, at 1).

Mr. Butler requested that the Commission undertake "additional dialogue . . . to shape the short term and long term needs of [the] wholesale electricity market[,]" rather than adopting the RPM. (*Id*. at 6). Notwithstanding New Jersey's policy objections, the Commission approved RPM because it disagreed with New Jersey's argument that "the [RPM] Settlement will raise prices without improving reliability." (Pl.'s Ex. 19, at 30); (T. 103, 11, through T. 104, 5).

In 2007, despite the Board's objections, the RPM rule was adopted which included the minimum offer price rule ("MOPR"). PJM subsequently adopted new rules on how the RPM would operate. These rules contemplated, among other things, who may enter into the RPM market and how each generator may bid

(T. 2653, 2-8). Most notably, the MOPR governed biddings by new capacity resources. Over the last several years, the MOPR has been modified several times by PJM in 2011 and 2013. Some of these modifications occurred based on the facts of this case.

The RPM Auction is not based on a pure open bidding process. For instance, an existing generator which previously operated as a part of a traditional utility is permitted to bid at zero. (T. 1652, 23 through T. 1653, 2). The rationale for permitting such bids is that these generation facilities have been operating longer than projected so capital costs have been recaptured. As such, the capital costs are deemed to be zero.[8] The ability of these long time generators to bid at zero when they may have sufficient capacity to provide to PJM raises a question as to whether the RPM Auction is actually necessary. In response to this question, PJM developed the MOPR, which it administratively calculates each spring from costs associated with the entry of a new generator; and then it lists administratively determined amount as the net cost of new entry ("net cone"). PJM converts that net cone into a price of megawatts per day ("benchmark price") (T. 1662, 17-19). While existing generators still bid at zero, they are accepting the net cone benchmark price in the RPM Auction. Hence, an existing generator became commonly known within the industry as a "price-taker." If such a generator forecasted that the benchmark price would fall below its projected cost, that generator may choose not to bid and retire the plant. (Def.'s Ex. 235). However, PJM was also concerned that new generators would bid below the

[8] Peculiarly, if a long time generator added more capacity to an existing plant, it may still bid at zero despite the development costs.

benchmark price in order to be accepted into the capacity market. Hence, MOPR was also a "mechanism that s[ought] to prevent the exercise of buyer market power in the forward capacity market by ensuring that all new resources are offered into PJM's Reliability Price Model (RPM) on a competitive basis." (Def.'s Ex. 331, at 4). In order to determine the competitiveness of a new generator, PJM applies a "MOPR screen." The MOPR screen has several components:

(i) a conduct screen (*i.e.*, a benchmark price used to determine whether a sell offer may be competitively low and thus warrants mitigation upward (described below); (ii) an impact screen test that compares the capacity clearing price with and without mitigation; and (iii) an incentive test, or net-short requirement (designed to distinguish between sellers who are net buyers and may have incentives to depress market clearing prices below competitive levels and sellers of planned generation who may have incentives to increase market clearing prices above competitive levels. (Def.'s Ex. 331).

Several exemptions applied to the MOPR's application including the "state mandated" and the "unit-specific" exemptions. When the MOPR was initially adopted, there was an exemption from the MOPR requirements if the project was undertaken pursuant to a state regulation or mandate (T. 1654, 12-15). According to Mr. Knight, a state mandated entrant could bid as an existing generator—price taker, and "bid whatever they wanted to bid." (T. 1654, 18). In addition, there was a unit-specific exemption applying to new gas-fired generation. Such unit-specific exemptions permitted bids down to 80% of the benchmark price upon a showing that the net cone

costs were at that level. Such a bid may be lower than the administrative benchmark price.

As noted above, the MOPR was changed through tariff modifications in 2011 (MOPR II) and 2013 (MOPR III). MOPR II eliminated the exemption that previously permitted developers of certain state-sponsored projects from bidding as "price takers." It also raised the "price floor" for new entrants' bids from 80% to 90% of PJM's benchmark price. (Def.'s Ex., at ¶¶ 24, 43, 66). According to Mr. Knight's testimony, in May 2013, the Commission further ruled that: (1) state-sponsored projects should be subject to the MOPR (which led the Commission to eliminate the "state exemption"); (2) the default MOPR level should be 100% of net cone; and (3) new projects should be allowed to demonstrate that their own projected costs will be lower than the benchmark price and should be able to pass a MOPR screen based on those projected costs. (MOPR III). (T. 1679, 20 through T. 1680, 3).

In addition to the MOPR screens, there was another accommodation for new entrants called the New Entry Price Adjustment ("NEPA.") (Def.'s Ex. 238). The NEPA provision was intended to make investments in new generation less risky. The NEPA assures developers of projects in local deliverable areas ("LDAs") that after their facilities become operational they will continue to receive, for a period of subsequent years, the capacity price of the RPM Auction that prevailed at their time of their entry. In 2006, concerns regarding how long the NEPA guarantee should operate were addressed by PJM and the Commission. PJM and FERC ultimately settled on a period of three years. (Def.'s Ex. 238). Despite the MOPR and NEPA adjustments, the RPM costs left New Jersey residents with higher electricity prices due to associated

transmission costs. These higher costs displeased the Board.

In addition to the RPM, two other energy issues arose in New Jersey at this time which adversely affected the industry and its regulations. First, PJM forecasted that the amount of energy required for New Jersey would be greater than the state's transmission capabilities potentially leading to outages. Notably, PJM identified twenty-three (23) power transmission violations which were likely to threaten PSE&G customers. Generally, these violations were deficiencies in service and reliability. (Def.'s Ex. 563, at 24-30); (Def.'s Ex. 567, at 20). The other adverse issue which arose was the adoption of new environmental regulations requiring that coal-fired plants be retired unless renovations substantially reducing emissions were made. As a result of these new environmental regulations, the Board projected that the amount of capacity within the PJM territory, particularly the amount of capacity in New Jersey, would be significantly reduced. Both of these adverse issues are discussed below.

Lack of Adequate Transmission Capabilities

In 2010, PJM disclosed to the Board that reliability issues may arise due to insufficient transmission capabilities in New Jersey. According to the PJM: "Based on the latest studies performed by PJM and the transmission owners, PJM, PPL and PSE&G concluded that there are 23 potential electric reliability violations that are expected to occur beginning in 2012, and extending out through PJM's 15-year planning horizon of 2022." (Def.'s Ex. 565, at 12). These violations had the potential to cause brownouts or blackouts. Since the violations were projected to occur within two or three years, the Board

became concerned about whether transmission capabilities could be improved in such a short period of time. PJM found that this reliability issue could only be addressed in one of two ways—increased transmission through the construction of the Susquehanna-Roseland transmission line ("Susquehanna Connection") or construction of additional generation in or near the location where the reliability violations would occur. (Def.'s Ex. 563, at 33). Given the difficulties associated with implementing either of these contingency plans in such a short period of time, from the Board's perspective, New Jersey was at risk. As Mr. Roach summarized, "this is really, to put it mildly [an issue that] . . . [got] their attention." (T. 1893, 22 through T. 1894, 2).

Environmental Issues

In 2008, newly imposed environmental regulations cast their shadow over the New Jersey energy industry when the federal and state governments partially prohibited coal-fired plants from being operated unless significant environmental modifications were made. At that time, federal environmental rules required 12 to 19 gigawatts of capacity in the PJM territory, which amounted to about 7 to 11 percent of all PJM generation, be retired or renovated. (T. 1612, 7 through T. 1613, 15). In addition, about a year later, New Jersey adopted the High Energy Demand Day Rule ("HEDD") which created a potential reliability issue by limiting the number of hours that certain electric generating units could operate. (T. 1897, 9-24). In short, from a resource adequacy or capacity perspective, the Board believed that New Jersey was vulnerable to the shutdown of 11,000 megawatts of coal-fired generation. (Pl.'s Ex. 127); (T. 1289, 22 through T. 1290, 9);(T. 1896, 21 through T. 1898, 10). As Mr. Roach explained it, the

Board thought, "I've got to put iron in the ground[.] I've got to get a new power plant locally to protect against these things." (T. 1894, 12-16).

G. INTRODUCTION OF THE LCAPP STATUTE

The Board undertook several measurers to address its concerns. First, the Board appealed the Commission's decision implementing the RPM and MOPR rules. Second, the Board worked with the New Jersey Legislature to develop a bill that would create new capacity resources closer to or within the State.

The Board's petition of review of the Commission's decision was summarily denied by the United States Court of Appeals for the District of Columbia. In its decision, the Circuit Court concluded "that the Commission had a substantial basis on which to conclude that the RPM was an appropriate tool for increasing reliability in electricity markets, that the RPM did precisely what it was intended to do, even during the transition period before the three-year lag could take effect, and that the price hikes in its wake were attributable to legitimate causes." *Md. PSC v. FERC*, 632 F. 3d 1283, 1286 (D.C. Cir. 2011). The Court did not specifically address the Board's or the State of Maryland's contentions regarding lack of reliability, the regional nature of increased capacity prices, or the impact of the newly implemented environmental regulations governing coal-fired plants. Rather, the court seemed to accept the Commission's determination that the "rates were just and reasonable" at face value. *Id*. at 1285.

On January 28, 2011, the New Jersey Legislature, with the Board's support, enacted the LCAPP Act which authorized the construction of several gas-fired generators in or near New Jersey. (Stipulated Facts

¶ 35). The purpose of LCAPP was "[t]o address the lack of incentives under the reliability pricing model" by fostering the "construction of new, efficient generation . . . [to] ensure[] sufficient generation is available to the region, and thus the users in the State in a timely and orderly manner[.]" N.J.S.A. § 48:3-98(d)(2); (Stipulated Fact ¶ 36). In general terms, the LCAPP Act established a "pilot program," overseen by the Board, to issue "Standard Offer Capacity Agreements" ("SOCAs") to selected eligible generators. N.J.S.A. § 48:3-98.3. The statute requires New Jersey's four electric distribution companies ("EDCs") to enter such contracts with eligible generators and obligates these EDCs to pay any difference between the RPM Auction price and their actual development costs approved by the Board. N.J.S.A. § 48:3-98.3(c)(9). The LCAPP contemplated the awarding of SOCAs for 2,000 megawatts of generation capacity. It further directed that the selected LCAPP generators were to "participate in and clear the annual base residual auction [RPM Auction] conducted by the PJM . . . for each delivery year of the entire term of the agreement." N.J.S.A. § 48:3-98.3(c)(12). In addition, the statute directed the Board to conduct a competitive solicitation of capacity and required winning bidders to enter into SOCAs lasting no longer than fifteen years with the State's electric distribution companies (EDCs). N.J.S.A. § 48:3-98.3(c)(1)-(4); *see also* (T. 121, 7 through T. 122, 24). The main purpose of the legislation was to provide a transaction structure that would result in new power plants being constructed in the PJM territory that benefit New Jersey. The New Jersey Legislature was ultimately interested in ensuring that new resources were constructed in time to help mitigate the reliability risks discussed above. N.J.S.A. § 48:3-98.2(b); *see also* (T. 1368, 17 through T. 1377, 1)

More specifically, the LCAPP statute required:

- that the Board hire an agent to: (1) "assist the Board with the establishment of the LCAPP program; (2) prequalify eligible generators for participation in LCAPP; and (3) recommend to the Board the selection of winning eligible generators based on the net benefit to ratepayers of each eligible generator's offer price and term." N.J.S.A. § 48:3-98.3(b)(1)-(3);
- that the Board "establish criteria associated with the prequalification of eligible generators in the LCAPP through a showing of environmental, economic, and community benefits, and through a demonstration of reasonable certainty of completion of development, construction, and permitting activities necessary to meet the desired in-service date" N.J.S.A. § 48:3-93.3(c)(6); (Stipulated Facts ¶ 39);
- that an "eligible generator" be "a developer of a base load or mid-merit electric power generation facility . . . that qualifies as a capacity resource under PJM criteria and that commences construction after the effective date" of the LCAPP. N.J.S.A. § 48:3-51; (Stipulated Facts ¶ 40);
- that a "Standard Offer Capacity Price ("SOCP") mean "the capacity price that is fixed for the term of the SOCA and which is the price to be received by eligible generators under a [B]oard-approved SOCA[.]" N.J.S.A. § 48:3-51. This price represents the development costs of the new generation as approved by the Board.
- that selected eligible generators "participate in and clear the annual base residual auction"

(RPM auction) for the sale of their capacity to PJM." N.J.S.A. § 48:3-98.3(c)(12); and

- that the Board order that New Jersey's four electric distribution companies (EDCs)—Public Service Electric and Gas, Atlantic City Electric, Jersey Central Power & Light and Rockland Electric Company "procure 2,000 megawatts of financially-settled SOCAs from eligible generation" for a period up to 15 years. N.J.S.A. § 48:3-98.3(c)(1),(9). The Board was further obligated to "establish a method and the contract terms for providing for selected eligible generators to receive payments from the electric public utilities for the difference between the SOCP and the RCP multiplied by the SOCA capacity." N.J.S.A. § 48:3-98.3(c)(4).

With the LCAPP, the New Jersey Legislature and the Board concluded that they would have to act to increase electric generation in the State due to the fact that the Commission's policies were not creating new capacity. As Dr. Roach noted in his testimony, the LCAPP created "some tension" between the Commission and the Board. (T. 2034, 25 through T. 2035, 1). One area of tension is summarized in the LCAPP. Within the statement of findings, the Legislature noted that the New Entry Price Adjustment was insufficient. It stated:

> The PJM reliability pricing model could, through structural changes, provide necessary incentives, such as the expansion of the "New Entry Price Adjustment" mechanism for the construction of new capacity, including new intermediate and base load plants, by allowing new resources to qualify and receive a guaranteed capacity

> price for a longer period of time. However, the implementation of similar structural changes was previously denied by FERC and any future implementation is uncertain at this time. N.J.S.A. § 48:3-98.2(c).

More specifically, the legislative findings declared that the Board would "allow new resources to qualify and receive a guaranteed capacity price for a longer period of time" than the RPM permitted. *Id*.

In addition, Board President Lee Solomon, in a September 16, 2010 memorandum to Governor Christie, affirmed that the purpose of the LCAPP was to establish a "multiyear pricing supplement" that would provide the new LCAPP generators with a premium payment or "RPM" adjustment that would guarantee a LCAPP generator a payment to secure multi-year capacity revenue." (Pl. Ex. 84, at 2). President Solomon also emphasized that the three year NEPA guarantee would be expanded to 15 years.

Moreover, LCAPP mirrors or overlaps the RPM Auction procedure. For instance, LCAPP requires that the price within a SOCA must be expressed in a "price per megawatt day" which is the same standard used in the RPM. *Compare* N.J.SA. § 48:3-98.3(c)(2) *with* (Stipulated Facts ¶ 8) (stating that "the price of capacity in RPM is generally measured in dollars per megawatt-day ("$/MW-day")).

Between 2008 and 2012, the transmission, reliability and environmental issues evolved. That is, many of the Board's concerns had subsided through the deliberate actions of PJM stakeholders and/or economic circumstances. As Mr. Roach characterized it, New Jersey "dodged a bullet." (T. 1894, 23 through 1895, 7). For example, PJM's reliability forecasts failed to

predict the 2009 recession, and therefore overstated the amount of capacity required. (Pl.'s Exs. 34, 65, 116, 275, 362). Accordingly, PJM reissued forecasts with lower usage estimates which minimized PJM's reliability concerns. During the trial, there was little to no evidence that this revised usage data proved to be false.

In addition, PJM recommended the construction of the Susquehanna Connection, a new 145-mile high voltage transmission line to move electricity from Berwick, Pennsylvania to Roseland, New Jersey. Presently, officials of PJM and PSE&G anticipate that construction on the project should be completed in 2014 or 2015. This project has the potential to solve the reliability violations that PJM projected. (Def.'s Ex. 563). Despite its ongoing construction, the Board argues that the length of time needed to complete the Susquehanna Connection project has left New Jersey vulnerable to outages. As such, according to the Board, new generation within New Jersey is needed to alleviate future reliability issues.

Lastly, the retirement of coal-fired plants has been an ongoing process. Despite the Board's concerns, PJM has found that within its territory the RPM had sufficient bidders to cushion or absorb the impact of these shutdowns. In addition, through the RPM Auction, PJM has acquired more than sufficient capacity to serve its territory. As PJM reported, although changes in environmental rules have led to significant retirements, "[t]he announced generation retirements sen[t] a strong signal that there would be a need for new resources, and [the 2012] auction witnessed a record number of new generation offers." (Def.'s Ex. 204, at 2); (T. 1084, 15-22). In fact, the 2012 RPM Auction cleared enough capacity to have a 20.2% reserve margin—significantly above the 15.4% reserve

margin usually reserved. It is noteworthy that one of the Board's witnesses confirmed that sufficient generation exists. Specifically, Mr. James Giuliano, Director of Reliability and Security of the Board, testified that he could not recall any power outages caused by insufficient generation. (T. 1104, 15-19).

Appointment of LCAPP Agent and MOPR Rules Revisited

In the first quarter of 2011, following enactment of the LCAPP, two significant events occurred. First, the Board appointed Levitan & Associates to be the LCAPP agent. (Pl.'s Ex. 136). Immediately after its appointment, Levitan began an exhaustive but expeditious selection process to identify generators capable of fulfilling both the requirements of the LCAPP statute and the policy objectives of the Board. Secondly, certain PJM stakeholders complained to PJM and the Commission that the state mandated exemption under MOPR should be prohibited because, under the exemption, the Board was unilaterally changing the price of capacity by imposing its own approved costs rather than relying on the competitive price of the RPM.

Levitan's evaluation of generators' proposals through the eligibility, prequalification and commercial proposal stages was based on an evaluation process "consistent with the LCAPP Law that [was] centered on the maximization of economic, environmental and community benefits from the standpoint of ratepayers in New Jersey." (Pl.'s Ex. 178, at 11). Specifically, "[a]pplicants were first reviewed in light of the requirements in the LCAPP Law to be an eligible generator. Eligible generators were then further reviewed to determine whether they should be prequalified on the basis of showing environmental,

economic and community benefits, and the demonstration of meeting the proposed in-service date with reasonable certainty." (*Id*.). Furthermore, "[t]he evaluation of commercial proposals was completed in parallel with the prequalification review." (*Id*.).

According to Mr. Levitan, the "community benefits" aspect of the prequalification assessment concerned "the developer's ability to drum up support in the community to achieve the [LCAPP Act's] aggressive [construction] milestones." (T. 1313, 7-15). The benefit sought was the timely construction of a qualifying new generation facility within the PJM territory. In evaluating the economic benefit of potential projects, Levitan "look[ed] at the completeness of the technology and operating data forms . . . [to] facilitate [its] analysis in the next phase." (T. 1312, 22 through T. 1313, 3).

In total, thirty-four (34) generation projects submitted prequalification applications to Levitan. (Stipulated Facts ¶ 43). Many of these projects were disqualified for various reasons. Notably, Levitan eliminated twenty-one (21) of the projects because they "were tied to existing generation units and therefore did not meet the condition of being a new generation facility." (Stipulated Facts ¶ 45). The Board and Levitan also eliminated four (4) projects because they "were characterized as peaking units, rather than base load or mid-merit units as required by the LCAPP." (Stipulated Facts ¶ 46). After three (3) generators withdrew their applications, only six (6) generators were prequalified. (Stipulated Facts ¶ 48). Of the six generation facilities that prequalified, Levitan recommended, and the Board later approved, that three be awarded SOCAs. These generators were Hess (625.0 MW of capacity), NRG (680.1 MW of capacity), and CPV (663.4 MW of capacity). (Stipulated

Facts ¶ 54). All three of these generator projects are located in New Jersey. (Stipulated Facts ¶ 52).

After the prequalification stage was completed, Levitan drafted the SOCA for each generator. The material terms of the three SOCAs are identical; they differ only with respect to the SOCA price, the quantity of capacity awarded, and the name of the generator. (T. 1368, 7-11). Herein the Court utilizes the SOCA of CPV as an example.

The Board awarded CPV a SOCA with a fifteen-year term. (Pl.'s Ex. 203). Each SOCA contains an Attachment F, which provides the schedule of Standard Offer Capacity Prices for the LCAPP generator for the fifteen-year term. CPV received the following price schedule:

| Delivery Year (ending May 31st) | Standard Offer Capacity Price ($MW-day) |
|---|---|
| 2016 | 286.03 |
| 2017 | 294.61 |
| 2018 | 303.45 |
| 2019 | 312.55 |
| 2020 | 321.93 |
| 2021 | 331.59 |
| 2022 | 341.54 |
| 2023 | 351.79 |
| 2024 | 362.34 |
| 2025 | 373.21 |
| 2026 | 384.41 |
| 2027 | 395.94 |
| 2028 | 407.82 |
| 2029 | 420.05 |
| 2030 | 432.65 |

Notably, CPV's SOCA has provisions which relate to PJM activity. For instance, the SOCA refers to the RPM, the RPM Auction and/or other actions that occur within PJM. (Pl.'s Ex. 203). The SOCA responsibilities which correlate to PJM activities are listed below:

> "Available Capacity Amount" means the lesser of: (i) the quantity of Unforced Capacity from the Capacity Facility that is offered by Generator and cleared by PJM in the relevant Base Residual Auction [RPM Auction], and (ii) the Awarded Capacity Amount.
>
> "Base Residual Auction" means the primary auction conducted by PJM as part of PJM's Reliability Pricing Model [RPM] to secure electrical capacity as necessary to satisfy the capacity requirements imposed under the PJM reliability assurance agreement for the Delivery Year.
>
> "Locational Deliverability Area" or "LDA" means the PJM sub-regions used to calculate Resource Clearing Prices as part of the Reliability Pricing Model.
>
> "PJM Interconnection, L.L.C." or "PJM" means the Regional Transmission Organization that manages the regional, high-voltage electricity grid serving New Jersey and all or parts of other states and, among other things, administers the Reliability Pricing Model, and any successor.
>
> "Reliability Pricing Model" or "RPM" means PJM's capacity-market model that secures capacity on behalf of electric load serving entities to satisfy load obligations not satisfied through the output of electric generation

> facilities owned by those entities or otherwise secured by those entities through bilateral contracts.
>
> "Resource Clearing Price" or "RCP" means the clearing price expressed in $/MW-day for Unforced Capacity established by the Base Residual Auction for the LDA in which the Capacity facility is located and the applicable Delivery Year as posted by PJM.
>
> "RPM Rules" means the provisions of PJM's tariffs and agreements accepted by the Federal Energy Regulatory Commission and the provisions of PJM's manuals governing the Reliability Pricing Model, as in effect from time to time during the term of this Agreement. (Pl.'s Ex. 203).

In addition to these terms, the term "delivery year" corresponds to the RPM availability requirement. Specifically, "Delivery Year" means "each 12-month period from June 1st through May 31st numbered according to the calendar year." (Pl.'s Ex. 203). The term is the same under the SOCA. The SOCA obligates the generator to qualify within the RPM by clearing the RPM Auction and acting in accordance with PJM rules. The SOCA dictates the procedure:

> 2.3.1. Generator shall use all commercially reasonable efforts to cause the Capacity Facility to qualify under the RPM Rules as a capacity resource in an amount no less than the Awarded Capacity Amount for the Base Residual Auction associated with each Delivery Year during the term of this Agreement, commencing upon the Awarded Commencement Date.

2.3.3. Throughout the Delivery Term, Generator shall:

(a) Cause the Capacity Facility to comply with all obligations of a capacity resource under the RPM Rules, including without limitation the obligations relating to the submission of offers to supply electric energy and ancillary services in PJM markets, and Generator shall bear all costs associated with such compliance, including without limitation all fees and penalties imposed by PJM;

(b) Submit supply offers for an amount of Unforced Capacity no less than the Awarded Capacity Amount from the Capacity Facility in accordance with the RPM Rules in the Base Residual Auction associated with each Delivery Year during the term of this Agreement, such that the Unforced Capacity shall be offered at the lowest commercially reasonable price under the RPM rules;

(c) Submit supply offers from the Capacity Facility for the maximum amount of Associated Energy that the Capacity Facility can provide in the PJM day-ahead energy market in accordance with PJM Market Rules throughout the Delivery Term, such that the Associated Energy shall be offered at the lowest commercially reasonable price under PJM' s Market Rules;

(d) Submit supply offers from the Capacity Facility for the maximum amount of Associated Ancillary Services that the Capacity Facility can provide in the PJM

ancillary services markets in accordance with PJM Market Rules throughout the Delivery Term, such that the Associated Ancillary Services shall be offered at the lowest commercially reasonable price under PJM's Market Rules;

(e) Neither physically nor financially withhold any Unforced Capacity up to the amount of Awarded Capacity, or Associated Energy and Associated Ancillary Services, from the Capacity Facility;

(f) Provide on a timely basis . . . (i) documentation provided to Generator by PJM after the conclusion of each Base Residual Auction showing the amount of Unforced Capacity offered from the Capacity Facility and cleared by PJM in such Base Residual Auction; (ii) documentation provided to Generator by PJM in advance of each Delivery Year showing all EFORd measurements for the Capacity Facility for the Delivery Year; (iii) the result of any capability test for the Capacity Facility conducted by PJM; (iv) documentation provided to Generator by PJM in advance of each Delivery Year showing the showing the Availability Capacity Amount for the Delivery Year or required to calculate the Available Capacity Amount for the Delivery Year; and (v) documentation notifying Generator of any correction to an input to a calculation." (Pl.'s Ex. 203).

The electric distribution companies have one broad obligation to the Board under the SOCA. (Pl.'s Ex. 203). That is, they must report their compliance with

the abovementioned obligations to the Board. The SOCA reads, in relevant part:

> 2.4. Obligations of the Utility. The Utility shall prepare and file an annual report to the Board within thirty (30) calendar days after the end of each Delivery Year describing (i) the status of this Agreement, (ii) the amount of Unforced Capacity and cost of associated Transactions made under this Agreement, (iii) the performance of the Generator in supplying Unforced Capacity and Associated Energy and Associated Ancillary Services under this Agreement, and (iv) any material actions taken by the Generator or the Utility under this Agreement. Nothing in this Agreement imposes upon Utility the obligation to monitor, enforce, or declare an Event of Default with respect to the price of Unforced Capacity, or the price or amount of Associated Energy or Associated Ancillary Services, which Generator offers in or supplies to any PJM Market. (Pl.'s Ex. 203).

In addition, the SOCA sets forth a formula to make payments or receive refunds based on the SOCA amount and the clearing price at the RPM auction. The SOCA states:

> 4.1.1. If, for a Delivery Year, the SOCP is greater than the [Recourse Capacity Price] then, subject to Section 2.5, Utility will pay Generator each Month during the Delivery Year one-twelfth of the product of (i) the difference between the SOCP and the [Resource Capacity Price], (ii) the Available Capacity Amount, (iii) the number of days in

> the Delivery Year; and (iv) Utility Load Ratio, each for the applicable Delivery Year.
>
> 4.1.2. If, for a Delivery Year, the [Resource Capacity Price] is greater than the SOCP then, subject to Section 2.5, Generator will pay Utility each Month an amount equal to one-twelfth of the product of (i) the difference between the RCP and the SOCP, (ii) the Available Capacity Amount, (iii) the number of days in the Delivery Year, and (iv) Utility Load Ratio, each for the applicable Delivery Year.
>
> 4.2. Structure of Transaction. Nothing in this Agreement shall entitle or obligate Utility to purchase, or take title to or delivery of, capacity, electric energy, or ancillary services from the Capacity Facility.

Under the SOCAs, "the LCAPP generators receive the payment set forth in the SOCAs only if they successfully sell the capacity from their facilities in the RPM base residual auction." (Stipulated Facts ¶ 56). The SOCAs also require the winning bidder to use all commercially reasonable efforts to construct an electric generation facility prior to the "commencement date" of its RPM obligation. (Stipulated Facts ¶ 58).

Finally, the SOCA requires that eligible generators maintain all approvals they have with PJM, and to "comply with Commission and RPM rules." The agreement sets forth:

> 6.2. Maintain Authorizations. Each party will use all reasonable efforts, including the maintenance of records and provision of notices, to maintain in full force and effect all

> consents, licenses or approvals of PJM and of any Governmental Authority or other authority that are required to be obtained by it with respect to this Agreement, the Construction Period Security, and the Delivery Term Security and its obligations hereunder and thereunder and will use all reasonable efforts to obtain any that may become necessary in the future.
>
> 6.3. Comply with Laws and RPM Rules. Each party will comply in all material respects with all Applicable Laws and orders and all RPM Rules to which it may be subject if failure so to comply would materially impair its ability to perform its obligations hereunder or under the Construction Period Security or Delivery Term Security.

In accordance with the terms of its SOCA, CPV (as well as the other two eligible generators) sought admission into the RPM Auction. According to Mr. Knight, as part of CPV's admissions process, representatives of CPV met with PJM to discuss the impacts of the MOPR II revisions and what information CPV would be required to submit. In response to a request for information issued by PJM, CPV sent an application consisting of more than 600 pages of materials. Within its application, CPV claimed it was exempt under the unit-specific exemption of MOPR II adopted in 2011, not the state mandated exemption provided for in the original MOPR. Under MOPR II, CPV could bid into the RPM auction at less than the minimum offer price floor (90 percent of net cone) if it could demonstrate that its actual costs were less than the benchmark price. (T. 1661:21 through T. 1673, 23); (Def.'s Ex. 51).

In determining whether CPV qualified for a unit-specific exemption pursuant to MOPR II, PJM did not consider any out-of-market payments that CPV would receive through New Jersey's LCAPP program. (Def.'s Ex. 183, 751); (T. 1674, 14 through T. 1675). Pursuant to its practice under the MOPR screen, PJM advised CPV that it would accept a bid of no less than $151.24 / MW-day, which is the level at which CPV bid. (T. 1678, 18-20). The May 2012 RPM Auction cleared at $167.46 / MW-day. (Def.'s Ex. 204); (Stipulated Facts ¶ 59). According to Mr. Knight, the RPM Auction price was different than the Board's approved costs due to "a difference in timing, and then secondarily a difference in the view on energy." (T. 1677, 12). With regard to the other eligible generator projects, Hess Corp's project cleared the auction while NRG's proposed project did not. Adamantly opposed, the four electric distribution companies signed the SOCAs under protest.

## H. IMPACT OF THE LCAPP STATUTE ON GENERATORS

Plaintiffs' witnesses testified that their respective companies rely on the forward price signals of the RPM Auction in deciding whether to develop new generation resources or make investments in existing resources within a specific market. According to these witnesses, the LCAPP makes it more difficult for these companies to make such business decisions because they can no longer rely on the RPM Auction price signals to evaluate their future costs and predict future revenue streams. In the view of the plaintiffs, the RPM Auction clearing price ($167.46) was essentially displaced and supplanted by the SOCA price written into the SOCA contracts ($286.03), causing less predictability in the energy capacity markets.

Zamir Rauf, Plaintiff Calpine's Chief Financial Officer, testified that the RPM Auction price signals play a "huge role" in Calpine's assessment as to whether an investment should be made because those prices are the basis for "projections as to where [Calpine] think[s] the market is going to be." (T. 1112, 3-14); (Def.'s Ex. 289, at 1). He expressed Calpine's reluctance to proceed with expansion plans in light of the LCAPP's enactment. In fact, according to Mr. Rauf, the LCAPP was a "very strong factor" in Calpine's decision to construct only half of its Garrison project as opposed to completing the project as originally planned. (T. 1121, 15 through T. 1130, 15). Mr. Rauf noted that Calpine was initially attracted to invest in the PJM region because it was a competitive market "where you can put your capital at risk, and compete based on your efficiency[.]" (T. 1114, 15-18 through T. 1115, 6-21). While Calpine "would love to invest more money into PJM[,]" as a result of the LCAPP, the company is now "taking a step back and just holding up from putting too much money into PJM . . .pending this uncertainty." (T. 1134, 8-12). Mr. Rauf summarized the conundrum for energy developers after the LCAPP's enactment:

> [T]he PJM market was designed with certain rules, and everyone has to play by the same rules. . . . [H]ow do you know the state two months from now or six months from now, a year from now, two years from now suddenly decides we need to create jobs let's build another power plant, or whatever political reason they may have for doing so. And all of a sudden they decide to build another plant, whereas you may have been in -- in the process of building one anyway or you may have started building one and now your

> capital's at risk because the price signals that were in the marketplace are no longer there because of this new plant, so it really just disrupts the whole marketplace, it just in my mind creates enough chaos to where you've got to be very cautious about putting money in a market where you don't know what the rules are, especially when the rules are being manipulated by the politicians. (T. 1130, 20 through T. 1131, 14).

As Mr. Rauf plainly stated, in light of the LCAPP, Calpine would "put[] less money in PJM than [the company] otherwise would have, and [Calpine] would probably either be reinvesting that money in other regions, or buying back [its] stock." (T. 1132, 6-12).

PSEG Power also had similar concerns regarding the impact of the LCAPP. According to Daniel Cregg, the LCAPP Act "dramatically change[d] how we look at what the market is." (T. 888, 20 through T. 889, 8). He noted that PSEG Power "shifted entirely away from . . . looking at it as a merchant opportunity" and began rationalizing that the "opportunity [was] not going to be there for [them] this year". (T. 879, 2-7). In the May 2012 RPM Auction, PSEG Power bid its Essex County project "at a fairly high level" in order to serve "as a backstop to the extent that the LCAPP units [did not] bid." (T. 886, 22 through 888, 12). In other words, "absent the LCAPP Act . . . there might have been a price signal that would have been there" for the Essex County project, but instead, "the LCAPP units did bid in, and as a result [PSEG Power's Essex] unit did not clear." (T. 887, 4-8).

The LCAPP also had an impact on the operations of Exelon, as discussed by Mr. Dominguez during his testimony. Specifically, he testified that the RPM price

signal "tells [Exelon] whether to make investments in existing plants; whether to increase the capacity of existing plants; whether to do environmental retrofits; [and] whether to keep plants open." (T. 527, 2-10). Mr. Dominguez further testified that, given its impact on Exelon's business strategies, the RPM is "fundamental to the way [Exelon] operate[s] [its] business." (T. 527, 8-10). In addition, Mr. Dominguez stated that the LCAPP Act has "fundamentally chang[ed] [Exelon's] ability to predict revenue streams for existing megawatts." (T. 564, 3-16). The LCAPP has also been a factor in Exelon's decision to place its nuclear uprate program on hold. (T. 564, 16).

PPL has also had to modify its business strategies in light of the requirements imposed by the LCAPP. Michael Cudwadie, Vice President for PPL EnergyPlus, testified that PPL relies on capacity forward market prices and energy forward market prices to make decisions regarding investments in new and existing generation, including whether to upgrade units, add pollution control equipment, or retire specific units. (T. 1041, 18-24).

The effects of the LCAPP described by these witnesses were echoed at trial by Plaintiffs' experts Mr. Massey and Professor Willig. For example, Mr. Massey declared that "[t]he entire fabric of the contract in my judgment makes it a price for capacity. It so happens that the contract calls it a standard offer capacity price, I . . . can hypothesize about a lot of things, but I don't know what can be clearer than that." (T. 296, 19-23). Mr. Massey elaborated by stating that "[t]he price is measured in terms of the netting of revenues, is measured in terms of comparing the standard offer capacity price, with the price determined in the PJM capacity market. It's all

about capacity pricing." (T. 298:2-10). Furthermore, the payments under the SOCA are "inextricably linked to the sale of wholesale capacity." (T. 298, 2-10).

Similarly, Professor Willig described the effect of the LCAPP as "wiping out the pricing mechanism of PJM . . . [and] taking it away and putting this alterative, the SOCA price, in the place of the market price." (T. 638, 22 through T. 639, 1). Professor Willig opined that the "architecture" of the RPM Auction was appropriately designed to address concerns in the energy capacity market (T. 763, 19-23) and that the RPM clearing price "is being displaced, . . . overridden, [or] supplanted, by the SOCA price through this mechanism which is written into the SOCA contract and governed by the LCAPP." (T. 637, 15-18).

Professor Willig further stated that the LCAPP would actually undermine new generation projects because all future investors would insist on receiving similar government assistance. He explained:

> Even though this is supposed to be an interstate market, the kinds of freedoms for the states, which they may have political incentives to act on, favoring their own development projects, will lead in a contagious way to other states taking measures that they think are only there in self-protection but are really their own reaction to the beginnings of this movement if the Court allows it, so that it's truly a contagion. We could very well be seeing a rash of programs of this kind, only furthering the rational insecurity of new investors who are not going to be part of these programs, fearing that the market will just be full of unfair competition

> for them, and thereby discourage their own investment activities. (T. 698, 11¬23).

Defendants' Perspective

The defendants have a completely different view concerning the impact and effects of the LCAPP based on two factual disagreements with the plaintiffs. First, the defendants contend that the RPM and the SOCA are two separate and unrelated transactions. The fact that each provides a different price does not, according to the defendants, frustrate the purpose or goals of the RPM Auction because, in their view, the SOCA is a purely financial contract not subject to Commission oversight and authority. Second, the defendants argue that any jurisdictional conflicts between the Board and the Commission were resolved by the Commission's 2013 MOPR revisions. Both of these arguments are addressed below.

According to the defendants, the RPM and the SOCA are unrelated. As Mr. Knight of CPV testified, the SOCA is "something separate and distinct." (T. 1646, 6-13). In describing this distinction, Mr. Knight elaborated that the "SOCA is between CPV and the EDCs, and does not go through PJM or have to do with PJM." (T. 1646, 6-13). He further pointed out that "[CPV] sell[s] physical capacity and energy to PJM," and does "not sell any physical capacity to anybody else." (T. 1644, 12-22). Mr. Knight distinguished the SOCA price from the RPM Auction clearing price by stating:

> The SOCA—I mean the general terms of the SOCA are relatively simple and straight-forward, but the obligation is for us to build a power plant, and to bid into, connect into PJM, and sell all our energy and capacity into

> PJM. And then in return for that we receive a financial payment from the EDCs, that is based upon a formula we're all . . . familiar with. It's a fixed price for a floating price, the floating price being the index in the PJM capacity market. (T. 1644, 12-22).

Defendants further contend that because the SOCA is a purely financial contract, it is not subject to Commission oversight. (T. 1911, 13-16). In fact, Defendants liken the SOCA to other financial contracts such as swaps, collars, or contracts for differences. (T. 682,2 through T. 683, 7). While the latter term (contract for differences) was mentioned frequently throughout trial, it was not fully defined except as an instrument that is routinely used to manage commodity price risks. (T. 1347, 1-15). For example, Mr. Levitan explained that a contract for differences is a "financially settled mechanism that provides revenue assurance for the seller and risk management benefits for the buyer." (T. 1282: 10-18). In the view of the defendants, because the SOCAs do not involve the sale of actual physical energy capacity, they fall outside the jurisdictional authority of the Commission. (T. 1282, 10-18). Mr. Knight agreed with this analysis and likened the SOCAs to insurance policies indemnifying against forced power outages. He testified:

> Because the payment mechanism is contingent upon something, it doesn't mean that we're delivering capacity . . . . [A]n example would be we have forced outage insurance in which we get paid by someone under a derivative contract if we are forced out. That doesn't mean that that's forced outages . . . it's just a contingency within the

> contract by which you get paid, it's not [like] you're actually delivering some good. T. 1648, 20 through T. 1649, 3).

So, under the defendants' analysis, the SOCAs are ultimately just financial risk management tools through which no capacity or energy is bought or sold. (T. 1283, 17-24); (T. 1360, 9 through T. 1369, 10); (T. 1644, 9 through T. 1645, 9).

With the adoption of the MOPR III revisions, the defendants argue that issues between the Board and the Commission concerning participation of new generators in the RPM Auction are resolved; and since there is no controversy between the Board and the Commission, there is no need for the Court to impose any remedy. The Court, however, rejects this argument for several reasons. Although the Board and the Commission may now have a more cooperative relationship, the Court is in the best position to determine whether the LCAPP and the related policies implemented by the Board violate the Supremacy Clause. In addition, despite the increased cooperation between the Board and the Commission, this remains a controversy between the plaintiffs (generators and distributors of electricity) and the Board.

Other Alternatives

Since the Board retained authority over the siting of generation facilities, a question arose as to whether the Board had any alternative means to incentivize construction of new generation facilities besides enacting a statute like the LCAPP. The parties agree that the Board had a number of ways to support and encourage the development of generation projects. These include the utilization of tax exempt bonding

authority, the granting of property tax relief, the ability to enter into favorable site lease agreements on public lands, the gifting of environmentally damaged properties for brownfield development, and the relaxing or acceleration of permit approvals. (T. 266, 25-26 through T. 267, 6); (T. 1313-14 through T. 1316, 2).

## I. CREDIBILITY OF WITNESSES AND WEIGHING OF THE EVIDENCE

As opposed to the facts set forth above, to which the Court has given considerable weight, the trial record reveals an extensive number of other facts which were given little weight in this decision. Those facts, and the reasons they were given little weight, are discussed below.

First, Defendants presented a plethora of facts about initiatives in Maryland and Connecticut which they believe present issues similar to those being considered in this case. The Maryland initiative is subject to a separate ongoing lawsuit. As Mr. Roach testified, it is based upon reimbursement of 400 megawatts of new demand response as opposed to a capacity requirement. (T. 2066, 20-24). Any analysis of the Maryland proposal would necessarily require this Court to review a set of facts as substantial as those presented herein. Based on the facts presented at trial, the Court is not able to discern whether Maryland's proposal is sufficiently similar to the LCAPP. As such, the Court considers the value in comparing and contrasting the Maryland initiative and the LCAPP to be minimal for purposes of this opinion.

In regards to the Connecticut proposal, the defendants contend that a Connecticut peaking facility has a very similar financial structure as a New

Jersey peaking facility under the LCAPP. (T. 1377, 24 through T. 1379, 11). Evidently, PSEG Power or one of its subsidiaries previously accounted for SOCA-like payments to a New Haven generator as financial contracts. According to the defendants, the payments in question were not listed as energy or capacity contracts required to be filed with the Commission. (Def.'s Ex. 630). The defendants argue that this supports their proposition that SOCAs are purely financial instruments. The Court, however, did not have sufficient information to fully analyze the Connecticut payments and, therefore, gave the defendants argument little weight. In the Court's view, the most compelling evidence regarding how the SOCAs should be defined under the law was adduced by the witnesses at trial. Therefore, in terms of credibility, the evidence regarding the Connecticut contracts was of little value.[9]

The Plaintiffs argue that certain written and oral statements allegedly made by Board staff and CPV executives are admissions against interest supporting the plaintiffs' case. Examples of these alleged admissions include:

a. Comments to President Solomon made by Frank Perrotti, Assistant Director of the Board, in which he stated that the LCAPP has the "potential to drive out other forms of investment or, at least, cause future

[9] On a motion *in limine* prior to trial, the Court ruled that the Connecticut initiative was not relevant because it involved a different state. During trial, the Court reopened that decision since the plaintiff's presented evidence involving initiatives in other states. The Court determined fairness required an evaluation of the Connecticut evidence.

developers to demand the same premiums before deploying capital." (Pl.'s Exs. 70, 406).

b. Comments made by President Solomon's aide Kristi Miller in which she stated that the LCAPP "could encourage future developers to demand identical premiums before deploying capital." (Pl.'s Ex. 406, at 20).

c. Comments made by CPV Chief Executive Officer Douglas Egan in which he indicated that in order to develop generation in New Jersey, a generator may need "out-of-market pricing" (Pl.'s Ex. 61) or "pricing that was higher than what was available at that point in time." (Pl.'s Ex. 409).

d. Comments made by the Board's Fed. R. Civ. P. 30(b)(6) designated witness, Mr. Dembia, in which he indicated that the LCAPP is a "guaranteed payout." (Pl.'s Ex. 406).

The Court gave little weight to these alleged admissions which occurred during the lobbying effort to enact the LCAPP. *See Kentucky W. Va. Gas Co. v. Pennsylvania Pub. Util. Comm'n*, 837 F.2d 600, 615 (3d Cir. 1988). The Court found that the witnesses at trial presented the facts and issues in a forthright manner. Since the statements were not subject to cross-examination, and could not be assessed for credibility, the Court believes the constitutionality of the New Jersey statute and program is best determined by reviewing the merits of the case rather than relying on isolated statements.

Plaintiffs also introduced a report prepared by the Brattle Group for purposes of showing the successes of the RPM. The Brattle Group is a consulting firm hired by PJM to evaluate the RPM. (Pl.'s Ex. 49). No one from the Brattle Group testified at trial. As a result,

the Brattle Group's report on the RPM Auction was not subject to cross-examination. As such, the Court gave the report little weight.

J. ANALYSIS

"Preemption is a doctrine of American constitutional law under which state and local governments are deprived of their power to act in a given area, whether or not the state or local law, rule or action is in direct conflict with federal law . . . . The analysis of a preemption dispute focuses upon statutory construction . . . in the context of a constitutional framework of sovereignty, commerce regulation, or other predicate for federal powers."[10] More specifically, preemption doctrine is rooted in the Supremacy Clause of the United States Constitution. Article VI declares that the laws of the United States "shall be the supreme Law of the Land; . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. art. VI, cl. 2. In order to determine whether the LCAPP is preempted under federal law, the first factual issue to resolve is whether the Board-ordered SOCAs occupy the same field of regulation as the Commission and intrude upon the Commission's authority to set prices for wholesale energy sales.

According to the defendants, the Commission's oversight authority is "limited to sales of the actual physical electricity (or capacity) to a buyer." (Def.'s Post-Trial Br. at 11). Furthermore, the defendants contend that "[c]ontracts that do not effect a physical sale of electricity . . . are not subject to [Commission] jurisdiction." (*Id*.). In the defendants' view, the SOCAs are purely financial contracts that do not involve

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[10] JAMES T. O'REILLY, FEDERAL PREEMPTION OF STATE AND LOCAL LAW: LEGISLATION, REGULATION AND LITIGATION 1 (2006).

physical sales of electricity.[11] As such, according to the defendants, the SOCAs are separate and unrelated to the RPM Auction process and free from Commission oversight. Plaintiffs argue, in opposition, that the "State, through the LCAPP Act and Board-ordered SOCAs, has set a price to be received for the wholesale sale of capacity to PJM." (Pl.'s Post-Trial Br. at 3). In the plaintiffs' view, the LCAPP ultimately "award[s] an impermissible price supplement for an interstate wholesale sale of electricity" and replaces the RPM price with the Board-ordered SOCA price. (*Id*. at 1). In doing so, according to the plaintiffs, the Board essentially sets a price for wholesale energy sales and, therefore, "regulat[es] in a field that is reserved exclusively" for the Commission. (*Id*.).

The Court finds that the SOCAs occupy the same field of regulation as the Commission and intrude upon the Commission's authority to set wholesale energy prices through its preferred RPM Auction process. As previously discussed, many of the terms defined in the SOCAs make substantial use of RPM terminology. In addition, the SOCAs obligate eligible generators to:

(1) "qualify under the RPM rules as a capacity resource in an amount no less that the Awarded Capacity Amount for the [RPM Auction]" (Pl.'s Ex. 203, at 9);

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[11] The Commission has previously held that "electricity price risk management transactions (futures, options, swaps, and the like)" that do not result in the actual delivery of electricity are "purely financial" and need not be reported to the Commission." *Morgan Stanley Capital Group, Inc*., 69 F.E.R.C. ¶ 61,175, 61,696 (1995).

(2) "comply with all obligations of a capacity resource under the RPM Rules" (*Id.*);

(3) "[s]ubmit supply offers . . . in accordance with the RPM Rules" (*Id.*); and

(4) "[s]ubmit supply offers . . . in accordance with PJM Market Rules[.]" (*Id.* at 9-10). The LCAPP Act itself defines the SOCA as a "capacity price . . . to be received by eligible generators under a Board-approved SOCA." (Pl.'s Ex. 127, at 10). Furthermore, payment of the SOCA price is made only if the LCAPP generators successfully sell and deliver wholesale capacity to PJM. Given the fact that the SOCAs require eligible generators' to satisfy certain RPM rules and mandate that the generators undertake certain performance under those rules, the Court finds that the performance of the SOCAs is contingent upon clearing the RPM Auction. As such, the SOCAs are not separate from, and to the contrary, occupy the same field as the RPM Auction.

"Under the Supremacy Clause, federal law may supersede state law in several different ways." *Hillsborough County v. Automated Med. Labs., Inc.*, 471 U.S. 707, 713 (1985). Specifically, the Supreme Court has recognized three types of preemption: express preemption, implied conflict preemption, and field preemption. *Id.* In this case, Plaintiffs argue that the Federal Power Act supersedes the LCAPP under both the field and conflict preemption theories.

Courts must begin their analysis of preemption questions by applying a presumption against preemption. *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 516 (1992). "In areas of traditional state regulation, we assume that a federal statute has not supplanted state law unless Congress has made such an intention 'clear

and manifest.'" *Bates v. Dow AgroSciences* 544 U.S. 341, 449 (2005) (citing *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co*., 514 U.S. 645, 655 (1995). "That assumption applies with particular force when Congress has legislated in a field traditionally occupied by the States." *Altria Grp., Inc. v. Good*, 555 U.S. 70, 77 (2008). Thus, when the "text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily 'accept the reading that disfavors preemption.'" *Id*. (citing *Bates*, 544 U.S. at 449). *See also Cipollone*, 505 U.S. at 518. Nonetheless, in the face of clear evidence, the presumption against preemption can be overcome. *See Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 374 n.8 (citing *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941). ("Assuming, *arguendo*, that some presumption against preemption is appropriate, we conclude . . . that the state Act presents a sufficient obstacle to the full accomplishment of Congress's objectives under the federal Act to find it preempted."). While applying the presumption against the preemption, the Court reviews whether the Federal Power Act preempts the LCAPP under either the field preemption or conflict preemption theories.

Field Preemption

Field preemption arises by implication when state law occupies a "field reserved for federal regulation." *United States v. Locke*, 529 U.S. 89, 111 (2000). The Supreme Court has explained that "[f]ield preemption reflects a congressional decision to foreclose any state regulation in the area, even if it is parallel to federal standards." *Arizona v. United States*, 132 S. Ct. 2492, 2502 (2012). This occurs when "Congress has left no room for state regulation of these matters." *Locke*, 529 U.S. at 111 (citing *Fidelity Fed. Savings & Loan Ass'n*

*v. De La Cuesta*, 458 U.S. 141 (1982). The Supreme Court has explained that a congressional intent to occupy a field can be inferred when "[t]he scheme of federal regulation may be so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947). It may also be inferred where "an Act of Congress 'touches a field in which [the] federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject.'" *English v. General Elec. Co.*, 496 U.S. 72, 79 (quoting *Rice*, 331 U.S. at 230). Nonetheless, because field preemption typically arises in areas traditionally regulated by states under their police powers, "congressional intent to supersede state laws must be 'clear and manifest.'" *English*, 496 U.S. at 79 (quoting *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977). Generally, "[t]he factors used to determine if the field has been fully occupied by federal power include the dominant federal interest, the expression of congressional purpose, and the pervasiveness of the federal regulatory system." O'Reilly, *supra* note 10, at 70.

Since the Supreme Court's 1927 decision in *Public Utils. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83 (1927), there has been a dominant federal interest over wholesale sales of electricity in interstate commerce. In that case, the Supreme Court invalidated an attempt by Rhode Island to regulate the rates charged by a Rhode Island plant selling electricity to a Massachusetts company, which resold the electricity to the City of Attleboro, Massachusetts. The Court found that the State's attempt to regulate rates "place[d] a direct burden upon interstate commerce" and, as a result, the "State [was] restrained by the force of the Commerce Clause." *Id.* at 89. Ever since

the Court's ruling, the federal government has asserted jurisdiction over wholesale sales of electricity in interstate commerce. As noted in Section E of this memorandum, in the absence of any federal regulatory body, interstate wholesale electricity pricing was left entirely unregulated after the *Attleboro* decision. In order to fill that regulatory gap, Congress enacted the Federal Power Act which provided that the Commission shall have jurisdiction over "the transmission of electric energy in interstate commerce" and "the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b)(1). *See New York v. FERC*, 535 U.S. 1, 20-21 ( 2002) ("It is clear that the enactment of the FPA in 1935 closed the '*Attleboro gap*' by authorizing federal regulation of interstate, wholesale sales of electricity—the precise subject matter beyond the jurisdiction of the States in *Attleboro*. . . . It is, however, perfectly clear that the original FPA did a good deal more than close the gap in state power identified in *Attleboro*. The FPA authorized federal regulation not only of wholesale sales that had been beyond the reach of state power, but also the regulation of wholesale sales that had been *previously subject* to state regulation.").

Plaintiffs contend that in enacting the Federal Power Act, Congress "chose to occupy the field of wholesale electricity sales, including the price at which electricity is sold at wholesale, and the terms and conditions under which such electricity is sold." (Pl.'s Post-Trial Br. at 12). Such a contention is supported by previous decisions in which courts have held that the Commission has the exclusive authority to regulate wholesale electricity sales and the transmission of energy in interstate commerce. As stated by Justice Scalia, "It is common ground that if FERC has jurisdiction over a subject, the States

cannot have jurisdiction over the same subject." *Miss. Power & Light Co. v. Miss. Ex rel. Moore*, 487 U.S. 354, 377 (1988) (Scalia, J., concurring in the judgment). The Supreme Court has held that the Federal Power Act "left no power in the states to regulate licensees' sales for resale in interstate commerce." *FPC v. S. Cal. Edison Co.*, 376 U.S. 205, 215 (1964). Moreover, the Court has repeatedly held that the federal statute "delegated to . . . the Federal Energy Regulatory Commission, exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce, without regard to the source of production." *New England Power Co. v. New Hampshire*, 455 U.S. 331, 340 (1982) (citing *United States v. Pub. Utils. Comm'n of Ca.*, 345 U.S. 295, 311 (1953). *See also Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 956 (1986) (stating that the Commission "has exclusive jurisdiction over interstate wholesale power rates."). The Third Circuit has similarly found that the "wholesale market for electrical energy is regulated by [the Commission]" and "[o]ne of [the Commission's] duties is to set 'just and reasonable' wholesale electric rates." *Utilimax.com v. PPL Energy Plus LLC*, 338 F.3d 303, 305 (3d Cir. 2004). The Commission's decision to exercise its exclusive authority to regulate wholesale electricity sales through the RPM Auction process indicates both a dominant federal interest in the RPM and a pervasive federal regulatory structure to ensure its proper implementation.

To support their proposition that the SOCAs are not "[c]ontracts . . . effect[ing] a physical sale of electricity" and, therefore, "not subject to [Commission] jurisdiction[,]" the defendants rely on the case of *New York Mercantile Exch.*, 74 F.E.R.C. ¶ 61, 311, 1996 F.E.R.C. LEXIS 454 (1996) ("*NYMEX*"); (Def.'s Post-

Trial Br. at 12). In *NYMEX*, the Commission held that the Federal Power Act and its reporting requirements did not apply to an electricity futures contract that was approved for trading by the Commodity Futures Trading Commission ("CFTC") except if the "contract goes to delivery, the electric energy sold under the contract will be resold in interstate commerce, and the seller is a public utility." *NYMEX*, 74 F.E.R.C. at 61,984. Without reviewing all of the facts of *NYMEX*, the Court finds the case distinguishable for several reasons. First, no evidence was presented to indicate that the SOCAs have been approved for trading by a separate federal regulator. Second, there is a caveat in *NYMEX* that if a contract "goes to delivery" it may give rise to Commission jurisdiction. Here, the SOCA agreements are contingent upon the LCAPP generators' successful sale of capacity to PJM. Such capacity sales may constitute delivery within the meaning of *NYMEX* and, therefore, give rise to Commission jurisdiction.

The most credible testimony presented at trial confirming that the SOCA contracts are not purely financial contracts, and that they, therefore, intrude upon the exclusive jurisdiction of the Commission, was that of Professor Willig. He explained that, in economics, a purely financial arrangement is one that does not "involve any real performance." (T. 681, 5-6). He elaborated that "[a] financial deal does not involve any performance of a real side activity as part of the deal. So that's really the dividing line, and I think it's quite clear, it goes back to what we mean by price in economics, payment for performance." (T. 681, 21-24). Here, the SOCAs expressly condition payment on physical performance. As Professor Willig explained, under the SOCAs, the LCAPP generator has "got to build a plant, it's got to provide capacity, the capacity

has to be available, had to be bid into RPM and into the auction, it has to clear the auction; there are all these elements of performance to which the SOCA payments are conditioned. So it's payment for performance." (T. 684, 10-15). Here, the LCAPP supplants the federal statute, and intrudes upon the exclusive jurisdiction of the Commission, by establishing the price that LCAPP generators will receive for their sales of capacity. The Court finds that in doing so, the LCAPP "places a direct burden upon interstate commerce" within the meaning of the *Attleboro* decision. Accordingly, the LCAPP Act invades the field occupied by Congress and is preempted by the Federal Power Act.

Defendants argue against preemption by stating that "Congress expressly reserved to the States exclusive jurisdiction to regulate generation." (Def.'s Post-Trial Br. at 23). According to the defendants, "State regulation of generation will not be pre-empted if the regulation's impacts on wholesale rates are merely 'incident of efforts to achieve a proper state purpose.'" (*Id*. (quoting *Nw. Central Pipeline Corp. v. State Corp. Comm'n of Kansas*, 489 U.S. 493, 515-16 (1989). Although the State of New Jersey and the Board retained the responsibility for the siting and construction of power plants, they are required to exercise this responsibility without interfering with the Commission's exclusive authority to regulate wholesale sales of electricity in interstate commerce. As discussed in Section H of this memorandum, there were other alternative measures which New Jersey could have employed to incentivize the development of new generation. While New Jersey retained the authority to take a wide range of actions to ensure reliable electric service for its citizens and encourage the construction of new electric generation facilities, it

chose to advance those goals through a mechanism that intrudes upon the authority of the Commission and violates federal law.

The defendants also contend that preemption analysis "does not justify a 'freewheeling judicial inquiry into whether a state statute is in tension with federal objectives." (Def.'s Post-Trial Br. at 23) (quoting *Chamber of Commerce of U.S. v. Whiting*, 131 S. Ct. 1968, 1985 (2011). Here, however, the Commission's exclusive authority over wholesale energy sales has existed since *Attleboro* and been confirmed by the Supreme Court and many lower courts decisions. An application of these prior decisions acknowledging the exclusive authority of the Commission to regulate wholesale electricity sales to the facts in this case certainly does not constitute "freewheeling."

Conflict Preemption

Conflict preemption occurs where there is a conflict between a state law and a federal law. *See Crosby*, 530 U.S. at 372 ("[E]ven if Congress has not occupied the field, state law is naturally preempted to the extent of any conflict with a federal statute."). Such a conflict occurs when "the challenged state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." 132 S. Ct. at 2501. When confronting arguments that a law stands as an obstacle to Congressional objectives, a court must use its judgment: "What is a sufficient obstacle is a matter of judgment, to be informed by examining the federal statute as a whole and identifying its purpose and intended effects." Crosby, 530 U.S. at 373. The court must look to "'the entire scheme of the statute'" and determine "'[i]f the purpose of the [federal] act cannot otherwise be accomplished—if its

operation with its chosen field [would] be frustrated and its provisions be refused their natural effect." *Id*. (quoting *Savage v. Jones*, 225 U.S. 501, 533 (1912)).

Where a state law conflicts with a federal law, the Court does not balance the competing federal and state interests. In fact, the Supreme Court has held that "[u]nder the Supremacy Clause of the Federal Constitution, '[t]he relative importance to the State of its own law is not material when there is a conflict with a valid federal law,' for 'any state law, however clearly within a State's acknowledged power, which interferes with or is contrary to federal law, must yield.'" *Felder v. Casey*, 487 U.S. 131, 138 (1988) (quoting *Free v. Bland*, 369 U.S. 663, 666 (1962)); *see also Gade v.Nat'l Solid Wastes Mgmt. Ass'n*, 505 U.S. 88, 108 (1992) ("[E]ven state regulation designed to protect vital state interests must give way to paramount federal legislation." (quoting *De Canas v. Bica*, 424 U.S. 351, 357 (1976)).

From reviewing the entire scheme of the RPM process, it is clear that the LCAPP Act poses as an obstacle to the Commission's implementation of the RPM. The testimonies of Messrs. Dominguez, Rauf and Cudwadie indicated that their companies rely on the competitive price signals of the RPM Auction to determine future company business plans. Each testified that the SOCA prices undermine their respective company's ability to use those RPM price signals to make sound business decisions. Each also contended that the future expansion of their respective companies would be contingent on whether the SOCA price continues to supplant the RPM Auction price. The effects described by the witnesses demonstrate that the SOCA's imposition of a government imposed price creates an obstacle to the Commission's

preferred method for the wholesale sale of electricity in interstate commerce.

Commerce Clause

The Plaintiffs argue that the LCAPP Act also must be invalidated under the Commerce Clause. This argument concerns the procurement of the capacity wherein Plaintiffs argue that Board discriminated against out-of-state generators in its solicitation of bids to become eligible generators under the LCAPP. The "dormant" aspect of the Commerce Clause prohibits states from using their regulatory power to discriminate in favor of in-state producers at the expense of those out-of-state. *C&A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 389-90 (1994); *W. Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 192 (1994); *Wyoming v. Oklahoma*, 502 U.S. 437, 454-55 (1992). The Supreme Court has defined forbidden discrimination as "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." *United Haulers Ass'n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 338 (2007) (quotation marks omitted): *W. Lynn Creamery*, 512 U.S. at 192.

When a law discriminates against out-of-state producers on its face, the State bears the burden of demonstrating, "under rigorous scrutiny, that it has no other means to advance a legitimate local interest." *C&A Carbone*, 511 U.S. at 392. "Statutes that discriminate by 'practical effect and design,' rather than explicitly on the face of the regulation, are similarly subjected to heightened scrutiny." *Tri-M Group, LLC v. Sharp*, 638 F.3d 406, 427 n.28 (3d Cir. 2011).

The plaintiffs argue that the "community benefit" points awarded to generators in New Jersey effectively prohibited out-of-state generators from competing to be eligible generators under the LCAPP Act. According to the plaintiff's, the LCAPP Act—through its express consideration of economic and community benefits—favored in-state enterprises over out-of-state enterprises." (Pl.'s Post-Trial Br. at 48). To demonstrate this, the plaintiffs rely on the following evidence: (1) President Solomon's letter to Governor Christie that mentions a preference for in-state generators (Pl.'s Ex. 84); (2) the initial draft of the LCAPP legislation that promoted construction of qualified in-state electric generators (even though such language was deleted prior to enactment) (Pl.'s Ex. 94); (3) language in the LCAPP which required the Board to consider the "economic[] and community benefits" of a project (Pl.'s Ex. 127); and (4) language in the 2011 New Jersey Energy Master Plan which discussed fostering the commercialization of new generation plants in New Jersey. (Pl.'s Ex. 270).

Despite the abovementioned evidence, the plaintiffs fail to overcome the most persuasive evidence that substantiates the reasons the State is seeking in-state development. A significant portion of the trial focused on locational deliverability areas (LDAs). (Stipulated Fact ¶ 30). As previously noted, New Jersey is located in such an area that is known as EMAAC. In addition, there are two other locational deliverability areas within New Jersey known as PSEG and PS North (T. 1529, 3-13). Generally, these LDAs have higher capacity prices than other PJM areas due to transmission costs. Even the Plaintiffs agree that a capacity price cannot be set for an entire region. (Pl.'s Ex. 26, at 34). As a result, there is separation in price which is authorized by PJM and the Commission. The

record as a whole supports the proposition that the closer the generation facility is to the delivery area, transmission costs will subside. As Mr. Herling concluded when discussing the reliability crisis, reliability issues could only be resolved in one of two ways—transmission via the Susquehanna Connection or additional *generation in or near the location where the reliability issue will occur*. (Def.'s Ex. 563, at 33) (emphasis added). As such, it appears reasonable that the Board would incentivize construction in areas where reliability concerns are in flux. As such, the Board has the authority to incentivize construction within New Jersey. What is good for the goose is good for the gander. As such, the incentive for community benefits to generators in New Jersey appears reasonable. Since Plaintiffs have not briefed or argued the commerce clause in such a fashion, the Court finds that Plaintiff has not met its burden of proof.

K. CONCLUSION

Based on the foregoing facts and law, the Court declares that the Long Term Capacity Agreement Pilot Program Act (LCAPP) is preempted by the Federal Power Act and in violation of the Supremacy Clause of the United States Constitution; and is therefore null and void.

*s/Peter G. Sheridan*
PETER G. SHERIDAN, U. S.D.J.

October 11, 2013

GLOSSARY OF ACRONYMS

| | |
|---|---|
| BGS | Basic Generation Service |
| BPU OR NJBPU | The Board of Public Utilities of the State of New Jersey; also referred to as "the Board" |
| BRA | Base Residual Auction |
| CC | Combined cycle |
| COD | Commercial Operation Date |
| CONE | Cost of New Entry |
| CT | Combustion Turbine |
| DAM | Day Ahead Market |
| DG | Distributed Generation |
| DR | Demand Response |
| EDC | Electric Distribution Company |
| EDECA | Electric Discount and Energy Competition Act |
| EE | Energy Efficiency |
| EMAAC | Easter Mid-Atlantic Area Council |
| EMP | Energy Master Plan |
| FERC | Federal Energy Regulatory Commission |
| FPA | Federal Power Act |
| FRR | Fixed Resource Requirement |
| GT | Gas turbine |
| GW | Gigawatt |
| GWh | Gigawatt hour |

| | |
|---|---|
| HEDD | High Energy Demand Day |
| ICAP | Installed Capacity |
| ISO | Independent System Operator |
| KW | Kilowatt |
| KWh | Kilowatt hour |
| LCAPP | Long Term Capacity Agreement Pilot Program |
| LDA | Locational Deliverability Area |
| LMP | Locational Marginal Price |
| LSE | Load Serving Entity |
| MAAC | Mid-Atlantic Area Council |
| MAAP | Mid-Atlantic Power Pathway |
| MOPR | Minimum Offer Price Rule |
| MW | Megawatt |
| MWh | Megawatt Hourf |
| NEPA | New Entry Price Adjustment |
| NERC | North American Electric ReliabilityCorporation |
| NRC | Nuclear Regulatory Commission |
| P3 | PJM Power Providers Group |
| PATH | Potomac-Appalachian Transmission Highline |
| PJM | PJM Interconnection, LLC |
| PPA | Power Purchase Agreement |
| RCP | Resource Clearing Price |

| | |
|---|---|
| RMR | Reliability Must Run |
| RPM | Reliability Pricing Model |
| RPS | Renewable Portfolio Standard |
| RTEP | Regional Transmission Expansion Plan |
| RTM | Real Time Market |
| RTO | Regional Transmission Organization |
| SIS | System Impact Study |
| SOCA | Standard Offer Capacity Agreement |
| TO | Transmission Owner |
| TRAIL | Trans-Allegheny Interstate Line |
| TRC | Total Resource Cost |
| UCAP | Unforced Capacity |
| VRR | Variable Resource Requirement |

**APPENDIX D**

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

[Filed October 25, 2013]

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Civil Action No. 11-0745
(PGS) (DEA)

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PPL ENERGYPLUS, LLC, *et al.*,

*Plaintiffs*,

v.

ROBERT M. HANNA, in his official capacity as President of the New Jersey Board of Public Utilities, *et al.*,

*Defendants.*

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JUDGMENT

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THIS MATTER, having been opened by way of Complaint for Declaratory Judgment and Injunctive Relief filed by Plaintiffs The PPL Parties[1], The Calpine Companies[2], Exelon Generation Company,

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[1] The "PPL Parties" include Plaintiffs PPL EnergyPlus, LLC; PPL Brunner Island, LLC; PPL Holtwood, LLC; PPL Martins Creek, LLC; PPL Montour, LLC; PPL Susquehanna, LLC; Lower Mount Bethel Energy, LLC; PPL New Jersey Solar, LLC; PPL New Jersey Biogas, LLC; and PPL Renewable Energy, LLC, which are marketing and generation subsidiaries of PPL Corporation.

[2] The "Calpine Companies" include Plaintiffs Calpine Mid-Atlantic Generation, LLC, Calpine New Jersey Generation, LLC, Calpine Bethlehem, LLC, Calpine Mid-Merit, LLC, Calpine Vineland Solar, LLC, Calpine Energy Services L.P., Calpine Mid-

LLC, Essential Power, LLC, Atlantic City Electric Company, PSEG Power, LLC, and Public Service Electric and Gas Company, and the Court, having heard testimony and otherwise received evidence at a bench trial held on April 2-4, 8-12, 18-19, May 6-9, and June 17, 2013, and having considered the submissions of the parties and the arguments of counsel, and for the reasons stated in the Court's Memorandum dated October 11, 2013, and good cause having been shown:

IT IS, this 25th day of October 2013;

ORDERED that, pursuant to this Court's Memorandum dated October 11, 2013, JUDGMENT is hereby entered in favor of Plaintiffs The PPL Parties, The Calpine Companies, Exelon Generation Company, LLC, Essential Power, LLC, Atlantic City Electric Company, PSEG Power, LLC, and Public Service Electric and Gas Company; and it is further

ORDERED that, pursuant to 28 U.S.C. § 2201(a), 28 U.S.C. § 2202, and 42 U.S.C. § 1983, this Court hereby declares that the Long-Term Capacity Agreement Pilot Program ("LCAPP") Act, P.L. 2011, c. 9 (Jan. 28, 2011) (codified at N.J.S.A. 48:3-51, 48:3-98.2 - 98.4), other than Section 5 thereof (codified at N.J.S.A. 48:3-60.1), violates the Supremacy Clause of the United States Constitution, U.S. Const., art. VI, cl. 2; and it is further

ORDERED that the Commissioners of the New Jersey Board of Public Utilities ("BPU") in their official capacities, and the employees and agents of the BPU, be and hereby are enjoined from enforcing or otherwise putting into effect any part of the LCAPP Act other than Section 5 thereof; and it is further

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Atlantic Marketing, LLC, and Calpine Newark, LLC, which are generation and marketing subsidiaries of Calpine Corporation.

ORDERED that the Standard Offer Capacity Agreements ("SOCAs") that Public Service Electric and Gas Company, Atlantic City Electric Company, Jersey Central Power & Light Company, and Rockland Electric Company signed under protest pursuant to BPU Order with Hess Newark Energy Center ("Hess"), NRG/NJPD Old Bridge Clean Energy Center ("NRG"), and CPV Woodbridge Energy Center ("CPV"), are void *ab initio*, invalid and unenforceable except for the termination provisions which any party may implement or defend; and it is further

ORDERED that Plaintiffs are entitled to costs pursuant to Federal Rule of Civil Procedure 54(d)(1) and Local Civil Rule 54.1; and it is further

ORDERED that Plaintiffs shall, in accordance with Local Civil Rule 54.1, file with the Clerk a Bill of Costs and Disbursements, together with a notice of motion when application will be made to the Clerk to tax the same, within thirty (30) days of the date of the Judgment; and it is further

ORDERED that Plaintiffs have withdrawn their request for attorney's fees in connection with the preemption claims in Court I of their Complaint and, as such, Plaintiffs' request for attorney's fees based on these claims is DENIED WITH PREJUDICE; and it if further

ORDERED that Defendants' Joint Motion to Stay Final Judgment Pending Appeal (ECF No. 311) is DENIED.

/s/ Peter G. Sheridan
Peter G. Sheridan, U.S.D.J.

Date: October 25, 2013

## APPENDIX E

Supremacy Clause

U.S. Const. Art. VI, Cl 2

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

# APPENDIX F

Federal Power Act, Section 201

16 USCS § 824

## § 824. Declaration of policy; application of Part

(a) Federal regulation of transmission and sale of electric energy. It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this Part [*16 USCS §§ 824* et seq.] and the Part next following [*16 USCS §§ 825* et seq.] and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce.

(1) The provisions of this Part [*16 USCS §§ 824* et seq.] shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this Part [*16 USCS §§ 824* et seq.] and the Part next following

[*16 USCS §§ 825* et seq.], over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(2) Notwithstanding section 201(f) [subsec. (f) of this section], the provisions of sections 203(a)(2), 206(e), 210, 211, 211A, 212, 215, 216, 217, 218, 219, 220, 221, and 222 [*16 USCS §§ 824b(a)(2), 824e(e), 824i, 824j, 824j-1, 824k, 824o, 824p, 824q, 824r, 824s, 824t, 824u, and 824v*] shall apply to the entities described in such provisions, and such entities shall be subject to the jurisdiction of the Commission for purposes of carrying out such provisions and for purposes of applying the enforcement authorities of this Act [*16 USCS §§ 791a* et seq.] with respect to such provisions. Compliance with any order or rule of the Commission under the provisions of section 203(a)(2), 206(e), 210, 211, 211A, 212, 215, 216, 217, 218, 219, 220, 221, or 222 [*16 USCS § 824b(a)(2), 824e(e), 824i, 824j, 824j-1, 824k, 824o, 824p, 824q, 824r, 824s, 824t, 824u,* or *824v*], shall not make an electric utility or other entity subject to the jurisdiction of the Commission for any purposes other than the purposes specified in the preceding sentence.

(c) Electric energy in interstate commerce. For the purpose of this Part [*16 USCS §§ 824* et seq.], electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale". The term "sale of electric energy at wholesale" when used in this

Part [*16 USCS §§ 824* et seq.] means a sale of electric energy to any person for resale.

(e) "Public utility" defined. The term "public utility" when used in this Part [*16 USCS §§ 824* et seq.] or in the Part next following [*16 USCS §§ 825* et seq.] means any person who owns or operates facilities subject to the jurisdiction of the Commission under this Part [*16 USCS §§ 824* et seq.] (other than facilities subject to such jurisdiction solely by reason of section 206(e), 206(f), 210, 211, 211A, 212, 215, 216, 217, 218, 219, 220, 221, or 222 [*16 USCS § 824e(e), 824e(f), 824i, 824j, 824j-1, 824k, 824o, 824p, 824q, 824r, 824s, 824t, 824u*, or *824v*]).

(f) United States, State, political subdivision of a State, or agency or instrumentality thereof exempt. No provision in this Part [*16 USCS §§ 824* et seq.] shall apply to, or be deemed to include, the United States, a State or any political subdivision of a State, an electric cooperative that receives financing under the Rural Electrification Act of 1936 (*7 U.S.C. 901* et seq.) or that sells less than 4,000,000 megawatt hours of electricity per year, or any agency, authority, or instrumentality of any one or more of the foregoing, or any corporation which is wholly owned, directly or indirectly, by any one or more of the foregoing, or any officer, agent, or employee of any of the foregoing acting as such in the course of his official duty, unless such provision makes specific reference thereto.

(g) Books and records.

(1) Upon written order of a State commission, a State commission may examine the books, accounts, memoranda, contracts, and records of—

(A) an electric utility company subject to its regulatory authority under State law,

(B) any exempt wholesale generator selling energy at wholesale to such electric utility, and

(C) any electric utility company, or holding company thereof, which is an associate company or affiliate of an exempt wholesale generator which sells electric energy to an electric utility company referred to in subparagraph (A),

wherever located, if such examination is required for the effective discharge of the State commission's regulatory responsibilities affecting the provision of electric service.

(2) Where a State commission issues an order pursuant to paragraph (1), the State commission shall not publicly disclose trade secrets or sensitive commercial information.

(3) Any United States district court located in the State in which the State commission referred to in paragraph (1) is located shall have jurisdiction to enforce compliance with this subsection.

(4) Nothing in this section shall—

(A) preempt applicable State law concerning the provision of records and other information; or

(B) in any way limit rights to obtain records and other information under Federal law, contracts, or otherwise.

(5) As used in this subsection the terms "affiliate", "associate company", "electric utility company", "holding company", "subsidiary company", and "exempt wholesale generator" shall have the same meaning as when used in the Public Utility Holding Company Act of 2005.

Federal Power Act, Section 205

16 USCS § 824d

**§ 824d. Rates and charges; schedules; suspension of new rates; automatic adjustment clauses**

(a) Just and reasonable rates. All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful. No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules. Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes. Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five month period. Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may

make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; "automatic adjustment clause".

(1) Not later than 2 years after the date of the enactment of this subsection [Nov. 9, 1978] and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources

(including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are—

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate

schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

Federal Power Act, Section 206

16 USCS § 824e

**§ 824e. Power of Commission to fix rates and charges; determination of cost of pro-duction or transmission**

(a) Unjust or preferential rates, etc.; statement of reasons for changes; hearing; specification of issues. Whenever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Any complaint or motion of the Commission to initiate a proceeding under this section shall state the change or changes to be made in the rate, charge, classification, rule, regulation, practice, or contract then in force, and the reasons for any proposed change or changes therein. If, after review of any motion or complaint and answer, the Commission shall decide to hold a

hearing, it shall fix by order the time and place of such hearing and shall specify the issues to be adjudicated.

(b) Refund effective date; preferential proceedings; statement of reasons for delay; burden of proof; scope of refund order; refund orders in cases of dilatory behavior; interest. Whenever the Commission institutes a proceeding under this section, the Commission shall establish a refund effective date. In the case of a proceeding instituted on complaint, the refund effective date shall not be earlier than the date of the filing of such complaint nor later than 5 months after the filing of such complaint. In the case of a proceeding instituted by the Commission on its own motion, the refund effective date shall not be earlier than the date of the publication by the Commission of notice of its intention to initiate such proceeding nor later than 5 months after the publication date. Upon institution of a proceeding under this section, the Commission shall give to the decision of such proceeding the same preference as provided under section 205 of this Act [*16 USCS § 824d*] and otherwise act as speedily as possible. If no final decision is rendered by the conclusion of the 180-day period commencing upon initiation of a proceeding pursuant to this section, the Commission shall state the reasons why it has failed to do so and shall state its best estimate as to when it reasonably expects to make such decision. In any proceeding under this section, the burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon the Commission or the complainant. At the conclusion of any proceeding under this section, the Commission may order refunds of any amounts paid, for the period subsequent to the refund effective date through a date fifteen months after such refund

effective date, in excess of those which would have been paid under the just and reasonable rate, charge, classification, rule, regulation, practice, or contract which the Commission orders to be thereafter observed and in force: *Provided*, That if the proceeding is not concluded within fifteen months after the refund effective date and if the Commission determines at the conclusion of the proceeding that the proceeding was not resolved within the fifteen-month period primarily because of dilatory behavior by the public utility, the Commission may order refunds of any or all amounts paid for the period subsequent to the refund effective date and prior to the conclusion of the proceeding. The refunds shall be made, with interest, to those persons who have paid those rates or charges which are the subject of the proceeding.

(c) Refund considerations; shifting costs; reduction in revenues; "electric utility companies" and "registered holding company". Notwithstanding subsection (b), in a proceeding commenced under this section involving two or more electric utility companies of a registered holding company, refunds which might otherwise be payable under subsection (b) shall not be ordered to the extent that such refunds would result from any portion of a Commission order that (1) requires a decrease in system production or transmission costs to be paid by one or more of such electric companies; and (2) is based upon a determination that the amount of such decrease should be paid through an increase in the costs to be paid by other electric utility companies of such registered holding company: *Provided*, That refunds, in whole or in part, may be ordered by the Commission if it determines that the registered holding company would not experience any reduction in revenues which results from an inability of an electric utility company of the holding company to

recover such increase in costs for the period between the refund effective date and the effective date of the Commission's order. For purposes of this subsection, the terms "electric utility companies" and "registered holding company" shall have the same meanings as provided in the Public Utility Holding Company Act of 1935, as amended.

(d) Investigation of costs. The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

(e) Short-term sales.

(1) In this subsection:

(A) The term "short-term sale" means an agreement for the sale of electric energy at wholesale in interstate commerce that is for a period of 31 days or less (excluding monthly contracts subject to automatic renewal).

(B) The term "applicable Commission rule" means a Commission rule applicable to sales at wholesale by public utilities that the Commission determines after notice and comment should also be applicable to entities subject to this subsection.

(2) If an entity described in section 201(f) [*16 USCS § 824(f)*] voluntarily makes a short-term sale of electric energy through an organized market in which the rates for the sale are established by Commission-approved tariff (rather than by contract) and the sale

violates the terms of the tariff or applicable Commission rules in effect at the time of the sale, the entity shall be subject to the refund authority of the Commission under this section with respect to the violation.

(3) This section shall not apply to—

(A) any entity that sells in total (including affiliates of the entity) less than 8,000,000 megawatt hours of electricity per year; or

(B) an electric cooperative.

(4) (A) The Commission shall have refund authority under paragraph (2) with respect to a voluntary short term sale of electric energy by the Bonneville Power Administration only if the sale is at an unjust and unreasonable rate.

(B) The Commission may order a refund under subparagraph (A) only for short-term sales made by the Bonneville Power Administration at rates that are higher than the highest just and reasonable rate charged by any other entity for a short-term sale of electric energy in the same geographic market for the same, or most nearly comparable, period as the sale by the Bonneville Power Administration.

(C) In the case of any Federal power marketing agency or the Tennessee Valley Authority, the Commission shall not assert or exercise any regulatory authority or power under paragraph (2) other than the ordering of refunds to achieve a just and reasonable rate.