ISSUES RELATING TO FEDERAL AND STATE JURISDICTION IN THE ELECTRICITY INDUSTRY

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Federal Power Act of 1935

Section 201(b)(1) provides that the Act applies to "the sale of electric energy at wholesale in interstate commerce" and that "[t]he Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction . . . over facilities used in local distribution or only for transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter."

Section 201 (c) provides that "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."

Section 201(d): "The term 'sale of electric energy at wholesale' when used in this subchapter, means a sale of electric energy to any person for resale."

Federal Power Commission v. Florida Power & Light, 404 U.S. 453 (1972): Florida Power & Light argued that it was not engaged in interstate commerce. It sold power to Florida Power Corp., which regularly exchanged power with Georgia Power at a "bus" south of the Georgia border. Supreme Court held that because power commingled in the bus moved across state lines, Florida Power & Light engaged in transmission in interstate commerce. To establish jurisdiction, the Commission need only show that "some [Florida Power & Light] power goes out of state."

Except for Alaska, Hawaii, or Texas, wholesale sales are in interstate commerce. Texas, which did not want to be subject to the federal oversight that comes with interstate electricity trading, created a separate grid covering most of the state, called the Electric Reliability Council of Texas (ERCOT). Members of ERCOT have pledged not to sell excess capacity beyond the state's borders in order to maintain avoidance of by FERC jurisdiction.

General rules:

- In 47 states, wholesale sales of electricity are in interstate commerce.
- FERC has exclusive jurisdiction over wholesale transactions.
- States may regulate retail transactions.

Public Utility Regulatory Policies Act of 1978 (PURPA)

Purpose: To reduce demand for fossil fuels and overcome utilities' traditional reluctance to purchase power from, and to sell power to, nontraditional facilities.

Method: Requiring utilities to purchase power from "qualifying facilities" (cogeneration facilities or small power production facility using renewable energy technologies) at rates based on the utilities' avoided cost.

Result: PURPA established the basis for independent, competitive companies to enter the power generation business.

States have no authority to order the modification of a qualifying facilities contract previously approved by FERC as final. Freehold Cogeneration Associates v. Board, 44 F.3d 1178 (3rd Cir. 1995).

States cannot require by rule that qualifying facilities contracts include a provision allowing state regulators to change the terms of the contract. Smith Cogeneration Management, Inc. v. Oklahoma Corporation Commission, 863 P.2d 1227 (Okla. 1993).

However, State regulator's onetime request for information not preempted by PURPA. Bristol Energy Corp. v. New Hampshire PUC, 13 F.3d 471 (1st Cir. 1994).

Energy Policy Act of 1992 (Amending §§ 211 and 212 of the Federal Power Act)

Purpose: To open and expand the wholesale transmission market and encourage the development of new competitive generating companies.

Section 211: "Any electric utility . . or any other person generating electric energy for sale for resale, may apply to the Commission for an order . . . requiring a transmitting utility to provide transmission services . . . to the applicant."

Section 212: "An order under section 211 shall require the transmitting utility . . . to provide wholesale transmission services at rates, charges, terms, and conditions which permit the recovery by such utility of all the costs incurred in connection with the [services]."

Exempt wholesale generators (EWGs) were exempted from the SEC acquisition review requirement under PUHCA (which sought to prevent the growth and extension of holding companies which bear no relation to "the integration and coordination of related operating properties.")

Utility companies became able to own EWG facilities, even outside their franchise area.

EPAct required utilities to open their transmission systems to other companies that sought to wheel power over them, but only for wholesale transactions (including sales to other utility companies and municipal power systems that resell the electricity to ultimate customers).

EPAct prohibited FERC ordering retail wheeling (shipments of power directly to the consumer).
(§ 722 of Title VII, Subtitle B)

FERC Order 888 (1996)

Order 888 sought to remove EPAct's requirement that independent power producers come in and ask FERC for access orders. FERC issued a single pro forma tariff describing the minimum terms and conditions of service to bring about this nondiscriminatory open access transmission service.

> All public utilities that own, control, or operate interstate transmission facilities were required to offer service to others under the pro forma tariff.
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> Order No. 888 also provides for the full recovery of stranded costs that were prudently incurred to serve power customers and that could go unrecovered if these customers used open access to move to another supplier.

FERC Order 2000 (1999)

Order 2000 requires all public utilities that own, operate or control interstate electric transmission to create or join a Regional Transmission Organization (RTO). The RTOs are to be operational by December 15, 2001.

The RTO concept evolved from attempts to remove barriers to open access and to ensure system reliability in a competitive marketplace.

Order 2000 contemplates that RTOs will have exclusive authority to maintain short-term reliability, including the right to order redispatch of any generator connected to transmission facilities it operates, if necessary for reliability:

> "In order to maintain the reliability of the transmission system, the entity that controls transmission must also have some control over generation. In general, we believe this control should be through a market where the generators offer their services and the RTO chooses the least cost options. This authority does not extend to initial unit commitment and dispatch decisions for generators. However, for reliability purposes, the RTO should have full authority to order the redispatch of any generator, subject to existing environmental and operating restrictions that may limit a generator's ability to change its dispatch."
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> "We intend the authority for generator redispatch to be used by the RTO to prevent or manage emergency situations, such as abnormal system conditions that require automatic or immediate manual action to prevent or limit equipment damage or the loss of facilities or supply that could adversely affect the reliability of the electric system, or to restore the system to a normal operating state."

RTOs would also have authority to override owner's scheduled outages. If an RTO operates within a region whose reliability standards are controlled by another entity (i.e., a reliability council), the RTO must report to the Commission if these standards hinder the RTO.

Pending Supreme Court Cases

The Supreme Court heard arguments on October 3, 2001, in two cases challenging FERC jurisdiction to regulate wholesale transmission services and power sales. (No. 00-568 and 00-809, October 1, 2001 term)

New York Public Service Commission v. FERC: Nine states (New York, Florida, Idaho, New Jersey, North Carolina, Virginia, Washington, Vermont and Wyoming) argued that FERC overstepped its authority with Order 888's requirement that utilities open their transmission lines to competing power merchants.

The states are appealing the District of Columbia Court of Appeals decision in Transmission Access Study Policy Group v. FERC, 225 F.3rd 667 (D.C.Cir. 2000) that upheld FERC's ruling that any transmission of third-party electric energy, including transmission on behalf of retail customers, falls exclusively within FERC jurisdiction. The court ruled that every third-party transmission service provided at any point along the privately owned, interstate-connected transmission grid is subject exclusively to federal regulation, even if the source of the energy and the consumer are located in the same state. Any delivery of electricity to a reseller (as opposed to an end user) constitutes FERC-jurisdictional transmission service, even to the extent that the facilities used to render the service include local distribution facilities.

Enron Power Marketing v. FERC: Enron argued that FERC violated federal law because it did not require access to transmission lines when utilities kept transmission and retail sales as one operation. This bundled service remains in many states where competition is not yet allowed. Enron contended that under the current access rules, a dominant utility in a state that has not moved to competition may keep power marketers from moving power across a region. (Associated Press, October 4, 2001)

Anomalies in Status Quo (Compiled by Scott Hempling)

State control over decisions with multi-state effects:

- Retail competition
- Power pools
- Environmental effects of electricity production
- Siting of transmission and generation facilities

Federal control over decisions with only in-state effects:

- Intrastate wholesale transactions
- Local transmission

Commerce Clause Issues

Article I, Section 8, Clause 3 of the United States Constitution, reserves to the Congress the power "to regulate commerce . . . among the several states." Although on its face the Commerce Clause merely gives Congress the power to regulate commerce among the states, "it has been settled for more than a century that the Clause prohibits States from taking certain actions respecting interstate commerce even absent congressional action." CTS Corp. v. Dynamics Corp. of America, 107 S. Ct. 1637 (1987).

State laws may violate the dormant Commerce Clause in two ways. First, statutes that clearly discriminate against interstate commerce and are not justified by a valid purpose unrelated to economic protectionism are unconstitutional. C & A Carbone, Inc. v. Town of Clarkstown, 114 S. Ct. 1677, 1682 (1994). Second, statutes that impose a burden on interstate commerce that exceeds the statutes' putative local benefits are unconstitutional. Pike v. Bruce Church, Inc., 397 U.S. 137, 90 S. Ct. 844 (1970).

The Supreme Court has applied (i) a rule of presumptive invalidity to regulations designed to further economic protectionism, and (ii) a balancing test, which is far more deferential to the states, to facially neutral regulations.

The negative or dormant commerce clause applies only where the state acts as a market regulator; it does not apply if the state acts as a market participant, similar to private actors in the market.

> Under negative or dormant commerce clause jurisdiction, state regulation that affords disparate, and less favorable, treatment to interstate commerce will ordinarily be struck down. Discrimination against interstate commerce in favor of local business or investment is per se invalid, save in the narrow class of cases in which a municipality can demonstrate under rigorous scrutiny that it has no other means to advance a legitimate local interest.
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> Nicholas Fels and Frank Lindh, "Lessons from the California "Apocalypse:" Jurisdiction over Electric Utilities," 22 Energy L.J. 1, 29 (2001).

Examples:

New England Power Co. v. New Hampshire, 455 U.S. 331 (1982): New Hampshire law that prohibited the exportation of inexpensive hydroelectric power to other states violates the Commerce Clause.

Pennsylvania v. West Virginia, 262 U.S. 553 (1923): West Virginia law that prohibited the export of natural gas by pipeline unless in-state needs had been met violates the Commerce Clause.

In re Nebraska Public Power District, 354 N.W. 2d 713 (S. Ct. S.D. 1984): State law that imposed an additional condition on the issuance of a permit for a transmission line, if less than 25 percent of the power transmitted over the line will serve that state, violates Commerce Clause.

Middle South Energy , Inc. v. Arkansas Public Service Commission, 772 F.2d 404, 416 (8th Cir. 1985): APSC may not prevent the utility from purchasing expensive power from an out-of-state nuclear plant in which it participates; the APSC cannot give a preference to its citizens by closing its borders to high-cost electricity, by shifting the burden to citizens of other states.

Issue: Does the Federal Power Act, by declaring that its provisions are not intended to displace otherwise proper state action, give states the affirmative authorization regulate in a manner that discriminates against interstate commerce?

> Tampa Electric Co. v. Garcia, 767 So.2d 428 (Fla. 2000), cert. denied, 121 S.Ct. 1227 (2001): Section 731 of the Energy Policy Act disclaims any intent to interfere with the authority of any State or local government relating to environmental protection or the siting of facilities. Florida Supreme Court concluded that Congress has granted the states leeway in the exercise of their siting authority to favor in-state usage, by requiring new plants to obtain a certificate of public need.

California S.B. 6, enacted on May 16, 2001, creates a financing authority to pay for electric generating facilities, to ensure a sufficient and reliable supply of electricity.

Section 3351 (a) provides:

> "All generation-related projects and enterprises financed pursuant to this division shall provide electricity to consumers of this state at the cost of generating the electricity, including the costs of financing those projects or enterprises. To the extent that electricity is not needed in the state, or that it is financially advantageous to California consumers, the electricity may be sold outside the state at just and reasonable rates."