

**“THE COURT HAS SPOKEN: WHAT DOES IT  
ALL MEAN?”**

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*S P E A K E R S*

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## P R O C E E D I N G S

MS. SUDA:

Good morning. I am Molly Suda. I am Vice Chair of the Professional Education Council and chair along with Gary Guy and Mosby Perrow. Welcome to the 2016 Annual Meeting. We have a very exciting lineup for you, a lot of interesting and engaging panels, starting off this morning with this morning's panel entitled "The Court Has Spoken: What Does It All Mean?"

I would like to invite our panelists up on stage, assuming they're all here. First we have Stu Caplan, Partner at Dentons. He will be moderating today's panel. We also have Clare Kindall, Assistant Attorney General from the Connecticut Office of the Attorney General. Max Minzner, over here, General Counsel for the Federal Energy Regulatory Commission. And Erin E. Murphy, a Partner at Bancroft PLLC.

Without further ado, I will turn it over to Stu Caplan for a panel that I'm sure will be very interesting.

MR. CAPLAN:

I'm a Partner at Dentons, and the organizer of this panel. This session, by the way, is being recorded for possible publication in the Energy Law Journal.

Before I go further, I just want to briefly introduce the panel, including one member who is a little bit late because of an accident on the highway, but she will be here shortly.

Max Minzner is the General Counsel of FERC. He is involved in the Commission's thought leadership on the issues implicated by three Supreme Court cases that were issued in 2015 and 2016, all concerning the dividing lines between state and federal jurisdiction, and federal preemption doctrine.

Prior to assuming his role as the General Counsel, Max was the Special Counsel to then Director of Office of Enforcement Norman Bay before he became Chairman. Max taught at the University of New Mexico School of Law and the Cardozo Law School. He has published in a number of publications, including Law Reviews of Harvard, University of Texas, and William and Mary. Max was also for a time an Assistant U.S. Attorney for the Eastern District of New York, and he is a native of Albuquerque.

Immediately to my right, Clare Kindall, is an Assistant Attorney General for the State of Connecticut. Clare has argued the *Hughes* case in the circuit courts—there are actually two circuit court cases that were related to this issue. And Clare is the head of the Energy Department for the Connecticut Attorney General's Office. She has argued many state and federal appeals.

She is also dealing with the aftermath of these cases, in particular the *Hughes* case which you will hear about, in terms of challenges to Connecticut State programs based on preemption arguments. Also, prior to public service, Clare served in private practice at Covington here in Washington, and in the Hartford office of Shipman & Goodwin.

Erin Murphy, who will be here shortly, is at Bancroft, a firm which is renowned for its Supreme Court practice. Erin was involved in two of these appeals, and took the lead on the briefs in both *Hughes* and *EPSA*.

Erin was a clerk to Chief Justice Roberts, and also to a U.S. Circuit Court judge. She has obvious insights on the inner workings from the Chief Justice's chamber. She also argued and won *McCutcheon v. FEC* in which aggregate campaign limits were held unconstitutional.

I think in the coming weeks we all may regret that decision. The National Law Journal named Erin as an Outstanding Woman Lawyer. Her namesake is an actress who played—and this I only learned last night when I was doing some background research—but her namesake was an actress who played the role “Bewitched” on TV. Erin achieved similar results, but without incantations.

The panel decided to launch right into a dialogue with some questions to focus the discussion, but before we do that I agreed to provide a common background so that we're all starting with the same fundamentals.

So very quickly, FERC Jurisdiction 101. FERC has jurisdiction under the Natural Gas Act over certain wholesale sales of gas, and over interstate transportation of gas. Under the Federal Power Act, FERC has jurisdiction over wholesale sales of electric energy—those are sales for resale, as opposed to end-use sales, and also over electric transmission in interstate commerce. And the Interstate Commerce Clause is satisfied by being anywhere on the interconnected grid in most situations.

Both statutes give FERC jurisdiction over rates, terms and conditions which affect those jurisdictional activities under what some persons would describe as the “Affecting” clause. And both statutes also preserve for the states jurisdiction over activities such as retail sales, or end-use sales of electric energy and natural gas, and over local distribution and, in the case of the Federal Power Act, over generation siting and certain related subjects.

The cases that we are going to discuss concern the convergence of FERC and state regulation, and also concern when states can be preempted.

There are two forms of preemption that we will be discussing. Field preemption is when Congress has fully occupied the field and there is no room for state regulation; whereas, conflict preemption can involve cases where both jurisdictions can regulate and the states can regulate similar subject matter to FERC, so long as the state regulation does not interfere with FERC regulation.

Now on to the three cases that we're here to discuss. I think in discussing with practitioners of equal and in some cases greater vintage, although there are fewer of those than there used to be, no one can remember a time in the last two or three decades in which the Supreme Court has issued three decisions in the course of one year which discussed the dividing lines between FERC and state jurisdiction.

Now the first of the three cases was *Learjet*, also referred to as *Oneok*. This case arose under the Natural Gas Act—here's Erin. You've been duly introduced. I'm just going through the three cases, and then we'll start with our first question. Great. Thank you.

The first of the three cases, *Learjet*, involved the alleged manipulation of natural gas price indices, which are of course used to price wholesale and retail sales of natural gas. FERC regulated the area, adopting regulations on this process. In three states end-use customers, retail customers, brought antitrust lawsuits concerning the same subject matter—that is, the alleged manipulation of the price indices.

The first district court to hear this case dismissed the case on preemption grounds. The Ninth Circuit did not agree and said, well, they were only seeking to go after the effects on the retail market, and the retail prices, so we reverse.

And the U.S. Supreme Court reversed and remanded because it found that the Ninth Circuit should have applied conflict preemption. That is to say that if these state lawsuits, or state regulations, did not interfere with FERC's regulation, then it would be okay for both of them to regulate the same subject matter.

The second of the three cases, *EPSA*, involved FERC's regulation of demand response in the electric market. FERC required ISOs and RTOs to offer full LMP [locational marginal price], full energy clearing prices, for economic demand response when it curtailed, in lieu of providing additional supply for the market.

The D.C. Circuit vacated FERC's rule, finding that demand response occurs in the retail market, and FERC had no place regulating in the retail market.

The Supreme Court reversed the D.C. Circuit, finding that FERC did not regulate the rates at which retail electric sales occurred, so that FERC did not step over the line of the subject matter preserved for the states under the Federal Power Act, and that it was okay for FERC to set the terms by which demand response would participate in the wholesale ISO markets.

The Court found that demand response affected wholesale sales and wholesale prices. It is not a small matter. In PJM in one year alone 10 gigawatts of demand response cleared the Capacity Auction and the Independent Market Monitor for PJM estimated that the aggregate capacity revenues that year were \$9 billion lower than they would have been without demand response. So it is a big business.

The third case is the *Hughes* case, also known as the *CPV* case—oh, before I move on, one thing about *EPSA* is that *EPSA* did not involve the review and attempt to invalidate state regulation under preemption. It was really decided on jurisdictional grounds. That is to say that FERC did not cross the line set in the Federal Power Act for states to regulate, and that since the activity affected the wholesale market FERC could regulate. But there was no state regulation that a party sought to invalidate pending before FERC or the Court in that case.

The third case, *Hughes*, or *CPV*, involved Maryland's decision to require contracts for differences. Maryland was concerned that there was not sufficient generation locating where and when needed, and adopted a program whereby the utilities had to enter into contracts for differences with generators that won some competitive solicitation process at the state level.

The case, the *Hughes* case, went before the district court, and then the Fourth Circuit, both of which found that the state was effectively setting the wholesale price of capacity and energy, and found that the state action was preempted.

And the Supreme Court affirmed, finding that Maryland had stepped over the line and was invading FERC's area of jurisdiction so that these contracts were invalidated.

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With that, it is time to turn it over to the panel. The disclaimer that you often hear applies to this session. So that you don't have to hear it four times, I'll say it once: The views that you are about to hear from each speaker are their personal views at this moment. They don't represent the views of any client, organization, agency, or anyone else. And we each reserve the right to change our views as early as later today. (Laughter.)

MR. CAPLAN:

Hopefully not in the same session. With state and federal regulations intersecting more and more, we need to provide some insight. We know from *Learjet* that practices affecting both retail and wholesale sales can be regulated by both FERC and the states, subject to preemption doctrine. But in *Hughes*, why didn't the Court reach the finding that states can regulate the generator incentives, including CFDs, as long as FERC has adequate tools to protect the integrity of the competitive marketplace?

Let me start with that question.

MR. MINZNER:

Well—I mean I'll start with it—it seems to me the Court obviously has a range of options whenever it is issuing an opinion, trying to draw the legal rule wherever it thinks it is appropriate.

It does seem to me that *Hughes* was very focused on the idea of preserving a wide range of tools for states to incentivize or affect generation, while being very focused on the specific attributes of those contracts for differences, including the bidding and clearing requirement, as well as the make-whole construction of those contracts that led to a very narrow decision about preemption.

MR. CAPLAN:

Okay. So in what ways was it narrow?

MR. MINZNER:

Well, the Court I think was clear that a significant number of traditional state activities that could in theory have an impact on the wholesale rate are likely to be preserved after *Hughes*. There's a long discussion at the end about the range of things that states can do without running afoul of the specific problem with constructs at issue in that case.

MR. CAPLAN:

Okay. Is there anything else to add?

MS. MURPHY:

You know, I think part of the important thing that the Court was looking at in *Hughes* was, there are kind of two lenses through which you could have thought about the cases is: What's going on in the regulation of generation? Or what's going on in the regulation, you know, interference with wholesale?

In a sense, I think the Court said, well, there's a little bit of both, and how do we think about a case that involves a little bit of both? And they seemed to come at that from the lens of, well, at the end of the day when what FERC is doing is within the scope of FERC's authority, then, you know, even if the states are, in a sense, within the scope of their authority, they can't get into that, that federal field. And I think that is why, you know, even though the Court kind of didn't deny that there was something going on that had to do with generation, and that generation is in a sense, you know, is something that is reserved to the states, and I think that's why you get all that important language at the end saying this doesn't mean states can't do things about generation, but it also doesn't mean that so long as you say this has to do with generation you're kind of out of the entire analysis of whether there might be a preemption problem.

MR. CAPLAN:

I find that there's an unsatisfying lack of clarity in the decisions as to the basis of jurisdiction in some cases, and as to the basis of preemption.

So, for example, in the case that we're talking about now, if the Court finds that the state was acting to stimulate generation where it thought it was needed, well that's reserved for the states. But at the same time, FERC has jurisdiction over wholesale prices for capacity and energy in the wholesale market.

So in that sense, this case might be viewed as involving matters that fall within the states' directly reserved jurisdiction, as well as FERC's directly assigned jurisdiction under the Federal Power Act. So it might be considered a "double direct case."

And in such situations, should field preemption apply? Or conflict preemption apply? And does it matter?

MS. KINDALL:

Well I guess I would say I'm relieved to hear that FERC's General Counsel thinks it's a narrow ruling, because I believe that the Supreme Court did narrow the Fourth Circuit's original holding.

But I also think that this is, the *Hughes* case and this trio of cases, is a full employment act for this room for the next ten years, because I think there will be a lot of litigation over what exactly a state can and cannot do.

There is really, I think for me personally, I think *Hughes* hinged on the issue that the Supreme Court really believed the states were setting wholesale rates, and thus directly invading an exclusive FERC jurisdictional area. But the states will need significant tools in order to encourage reliable and clean energy in specific local areas. And the question will become: Where can the state do that?

And I think that litigation—in fact, Connecticut currently is in the middle of litigation on this exact issue. And so I think there will be a large number of cases that will emerge about where are those lines going to be drawn. And I believe the Federal Power Act is really designed for cooperative federalism. You know, there is a role for FERC and there is a role for the states. And this room will spend most of the next ten years drawing those lines.

MS. MURPHY:

One of the things that's striking to me, when you look at the three cases kind of as a trilogy, I really think that the takeaway is the Court was trying to avoid drawing particularly bright lines that are giving a whole lot of guidance. It really kind of approached each of the cases as we're going to resolve precisely what's before us, and not say a whole lot more than that, which isn't all that unusual for how the Court operates, particularly when it's dealing with an area like this where, you know, the Court knows it's not the body with the great expertise on all this, but at the same time I think it's probably quite frustrating for people who practice in this area because I'm not sure, you know, the opinions are sort of designed to say we are going to look at each of these a little bit on a case-by-case basis, and look at these factors, and it's going to depend on the particular program. And we have written these opinions in a way that tells you, well, they don't necessarily strike down the next thing, but they also don't necessarily tell you the next thing is okay, either.

So I think you're absolutely right, that this is probably going to put an end to litigation in this area.

MS. KINDALL:

And the Scalia dissents. I mean, Scalia was, you know, Justice Scalia was all about bright lines, and we're saying there are no bright lines here, and I think in *Hughes* he would have ruled with the other eight, but that—against us, I might add—but I think that he was about bright lines, and I think that there is an awful lot to be said about a more nuanced case, even though it is going to keep us all employed for a long time.

MR. CAPLAN:

Justice Scalia's warning in the dissent in the *Learjet* case, was that now gas pipelines will be subject to regulation by FERC on the same subject matter by which they're now subject to regulation by fifty states, and perhaps fifty state court systems and juries. And that was troubling to him.

So I think that the advertisement for future litigation in this field, and a gift for this Energy Bar that I would personally not wish on anyone, remain facts—there is a need for future clarity.

Let's shift for a moment to the challenges that states face going forward. We know that the Clean Power Plan is the subject of a stay, but a lot of states are engaging in planning to satisfy their required greenhouse gas reductions.

And the EPA regulation assumed that each state's nuclear power plants that were operating would, generally speaking, continue to operate.

Meanwhile, there's concern in some markets that nuclear power plants did not derive sufficient revenue from ISO and RTO wholesale markets to make the capital expenditures necessary to keep the plants running.

Additionally, state programs to stimulate renewable energy—so here you have two potential zero carbon emission sources, nuclear power and renewable energy—may not derive sufficient revenue from the markets such that they need certain forms of subsidies or incentives. And those have come at the state level.

So is it okay for a state to establish REC prices? Or to administer a market for REC prices? That's setting a price for wholesale sales. Is it okay for a state to adopt a program to supplement the revenue that a nuclear power plant receives because it would be very hard to satisfy the carbon reduction targets of the EPA rule without the nukes?

Let me throw that out to the panel. What should a state do? And what shouldn't it do? What is clearly okay, if anything, and what is going to be subject to that litigation you have just been talking about?

MS. KINDALL:

Well, Connecticut is doing a large number of RFPs as we speak. And so—again with the caveat this is entirely 100% my own personal views—I believe that the Court laid out, you know, various subsidies that could be done. I think as long as it is, quote/unquote “untethered” from the wholesale market, a deregulated state can do bilateral contracts like the Morgan Stanley contracts. They can do subsidies. They can do all kinds of other supports and subsidies. And the Court was pretty clear on that. And bilateral contracting is long established as being separate from the markets.

That said, I think that there are—there needs to be a fundamental look as to whether or not markets answer all questions. The markets have done a tremendous good, and Connecticut is deregulated and was a little offended at the idea that the only way to sort of ensure reliable energy was to reregulate, which was one of the suggestions at the end of *Hughes*: Well, you can always reregulate.

And that struck us as really the wrong tack to take. It struck me as the wrong tack to take. And so the question becomes: If you have a market—do you have a market failure? And if you have a market failure, how do you address it?

And I think that is going to have to be a cooperative thing between the federal agencies and the state agencies. I think the one lesson from these three cases is that, you know, if FERC decides it has jurisdiction, then FERC is going to probably be supported in that.

I think if FERC had come out the other way in *Hughes*, *Hughes* would have come out differently. But I think there is a real partnership to be had between the Federal Government and the state governments. And with that sort of cooperative working together, I think they can make it work. But I think the first step will be to see: Is the market working or not? And if the market is not working, what is the best way to address it?

MR. MINZNER:

So let me start with what Clare did. My remarks of course are my own, as well, and not the views of the Commission or any of the Commissioners.

I will say that I think *Hughes* did preserve a lot of room for state activity. I think the bilateral contracting for capacity language, noting that capacity that transfers outside the auction doesn't run into the same preemptive issues that the state subsidies that were at issue in *Hughes* had is an important caveat.

Certainly the notion of REC programs are not a new innovation in the energy markets. They've been around for many, many years without being preempted. And it is hard to see those as having exactly the flaw that the market issues had in *Hughes* itself. It's hard to pass on any program in the abstract, of course, but there certainly is a wide range of room preserved in *Hughes* for state activity.

MR. CAPLAN:

In *Hughes* one of the factors considered was that the prices of the CFD had the effect of looking into, or reviewing the wholesale market revenues that the generator would receive, and then supplementing or subtracting from those based on the contract for differences strike price.

So the pricing was tied to the wholesale market prices, and the Court viewed that as supplanting FERC's establishment of a market to establish those prices. So if you have, for example, a subsidy that is geared towards keeping a power plant that's low-emission, that you want to continue to have running, would you say that it would be more problematic if the state pegged the revenues that that plant might receive to the market revenues? Assume a state takes the position it does not want to overcompensate the generator by guaranteeing \$10 million a year, or \$15 million a year, rather the state rules it will only give the generator money to the extent that its market revenues are below  $x$ . Would that be similar to one of the issues that the Court found problematic in *Hughes*?

MS. MURPHY:

I think it would raise a concern under the way the Court was thinking about it, which was, you know, I mean if what you're doing effectively amounts to looking at what the market as established by FERC is going to give you, and having the state decide you should get something different, I mean I think that was kind of the core of what the Court seemed to think was problematic.

Now I think this also gets at why, you know, maybe that's not quite as narrow of a concern as they seem to think that it was in *Hughes*, given the facts before it, and maybe if the program were set up a little differently they might look at it a little differently, but that does seem, when you look at what they were talking about in the issue, the kind of two issues that come up over and over again, are that it was, you know, pegged to the market and that it was pegged to a market where FERC had already decided that there was a process which would produce the Just and Reasonable Rate.

So it wasn't kind of just a wholesale transaction in the abstract. It was one that was already regulated by FERC before it ever happened. So I think anything that kind of pegs itself directly to that rate in the auction has the potential to raise the concern that was animating the Court in *Hughes*.

MS. KINDALL:

I agree with Erin. I think under this Court's ruling I think pegged to the market is going to raise some flags. However, then the question becomes do the ratepayers pay twice? And how do you avoid ratepayers paying twice for the energy they need, and then paying again for the sufficient to meet the various goals in the market.

And I think those are difficult questions on how you work out that balance.

MR. CAPLAN:

I'm not sure it's clear to everyone what you mean by "the ratepayer pays twice"? Why would the ratepayer pay twice?

MS. KINDALL:

If the market—if you're paying for energy that doesn't clear the market, and you still need to make a certain amount in the market, then the ratepayer pays both for the market—for the subsidy, or for the energy they have supported to have reliable or clean energy, and then but they also need to pay for energy to be in the market up to a certain level. So the ratepayer pays twice.

And that really was the whole purpose behind the contract-for-differences mechanisms, which I think are pretty well shot at this point. I think that, though why you can do a contract for different—the state can't do a contract for differences, but Merrill Lynch can. I'm not quite sure I understand that.

But that said, the whole purpose of that structure that Maryland and New Jersey have put in was to avoid the ratepayer paying twice. And, you know, I think there was a real social good to that.

That said, it certainly was, quote/unquote, "tethered" to the market. And I think we'll be spending a lot of time trying to figure out what "untethered" and "tethering" means for the next couple of years.

MR. CAPLAN:

On that front, it seemed as though the Supreme Court found objectionable some combination of the following factors:

First, the states mandated that the utilities or distribution companies enter into these contracts with the generators;

Second, the prices were tied to the wholesale market prices in a way that effectively set the price the generator would receive for wholesale capacity and energy in Maryland, or just capacity in New Jersey if you were looking at that case;

Third, the generator had to clear the PJM Capacity Auction so that, in Clare's words, the load would not pay twice, once through the CFD for capacity that wouldn't count. If the generator didn't clear the Capacity Auction, that new 750-megawatt power plant might have zero capacity credit and the load would not only have to pay for the CFD but also pay in the PJM Auction for other capacity to satisfy its requirement. And therein would be double-paying.

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So the Court found some combination of those objectionable. But I postulate that the Clear Requirement—that is, the requirement that the generator clear the auction in order to be eligible for the CFD—is something that, and we’re just using Morgan Stanley as the hypothetical financial institution in this dialogue not as an advertisement or otherwise, but that Morgan Stanley would be well served with the Clear Requirement because if the strike price in the CFD were \$200 per megawatt/day, and the market cleared at \$300, the generator would owe Morgan Stanley \$100 per megawatt/day times 750 megawatts times 365 days a year. That’s a lot of money.

If the generator clears the auction and receives the auction revenue, then its collateral and security requirement to provide assurance to Morgan Stanley would be understandably lower.

So if that were problematic in itself, then I think the financial institutions might be looking at this issue not just as an issue affecting a state, but perhaps influencing private financial institutions as well.

MS. KINDALL:

That might have helped us with the Amici side.

(Laughter.)

MR. CAPLAN:

I want to shift for a moment, because we haven’t discussed Demand Response. I mentioned *EPSA*. We haven’t given *EPSA* sufficient attention yet. *EPSA*, again, was the case where FERC required ISO/RTOs to provide full LMP for Demand Response that curtailed load. The D.C. Circuit threw it out because it said, FERC, you don’t have jurisdiction. It’s in the retail market. The Supreme Court said, no, you’re not regulating a retail price. So, FERC, it’s okay to regulate if it directly affects the wholesale price. But it wasn’t a preemption case.

So what do you panelists think a state can or can’t do? Is it okay for a state to regulate in Demand Response now that FERC has jurisdiction over its offer into the wholesale market? And if so, are there any limitations on that state regulation you think might apply?

MR. MINZNER:

It seems to me that the place to start, if you’re thinking about the scope of state authority, is not with *FERC v. EPSA*. It’s with *Oneok* and *Hughes*. Those are the cases that are about the limitations on state authority. *FERC v. EPSA* is fundamentally a question about the scope of the Federal Power Act, the extent of the statutory power of the agency. Those are related questions, but I don’t think they’re identical. And it seems to me that you just start in a different place if you’re asking about what states can do and what the Federal Government can do.

MS. MURPHY:

I think that’s right, but I mean it is worth noting that one of the reasons the Court identified for coming out the way it did in *EPSA* was it said if FERC can’t regulate this in the wholesale market, then who can? Because it assumes the states couldn’t.

That was actually kind of one of the three prongs of the Court's analysis, was to say precisely because this DR is going on in the auctions, you know, we're assuming that states couldn't be there even if they wanted to, and we're worried there would be a regulatory void there.

So in a sense they kind of looked at the scope of FERC's authority through this slightly, you know, backward way of saying, well, if the states don't have the authority, and we think they don't, then it must be that FERC has the authority because someone must have the authority, which of course was one of the features in the dissent in *EPSA* as a point with which the dissent disagreed, that there needs to be one body that has the authority or not. But it seemed to be a feature of how they thought about it.

MS. KINDALL:

And I would agree with both Erin and Max on that. I will note that the states weighed in on the side of FERC in *EPSA* because we were all facing a fairly large concern that Demand Response would disappear from the wholesale markets and there would be pretty significant financial consequences to that.

And the states really weren't involved in the lower levels of that. The issue kind of snuck up on people and suddenly there was a D.C. Circuit decision that had great language for the states—I mean, we loved the analysis—but it really left us with a policy concern of: Oh, no, what are we going to do if Demand Response is eliminated from all these wholesale markets that no one was really willing to face?

MR. CAPLAN:

Well I think that the states are free to regulate Demand Response in the retail context.

MS. KINDALL:

Agreed, yes.

MR. CAPLAN:

But if the state regulation interferes with FERC's regulation of wholesale Demand Response, Demand Response offered into the wholesale market, then would preemption apply or not?

MS. KINDALL:

Is it tethered, or untethered?

MR. CAPLAN:

Well why don't we define what "tethered" and "untethered" mean in this context. If a state were to adopt a rule, for example, that said: Well, we're not going to allow our end-users to participate in Demand Response categorically, would FERC be able to say, oh, sorry, we're going to preempt you in that?

As opposed to a state saying: If a Demand Response participant decides to curtail its load, we're not going to give it a break on its retail bill for its Demand charge because we don't want to stick other customers with that cost shift.

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Those are two fundamentally different ways a state could regulate Demand Response. One of them, arguably indirectly affects wholesale market participation, and one of them directly.

I'm just throwing this out here on the fly, but what do you think the outcomes might be, or the issues might be in both of those contexts?

MS. MURPHY:

It gets a little to one of the arguments that we, representing the challengers in the *EPISA* case, made. Which was, you know, FERC has structured its rule to accommodate states that don't want to participate in certain respects, and we made the argument that that kind of should demonstrate to you that it's not within FERC's jurisdiction under kind of field preemption principles.

And given that the Court didn't accept that, I think what then that means is you move on to thinking about it through kind of a conflict preemption lens, and thinking about, you know, is there a way in which it interferes with the objectives, and all of that.

And I think at that point it would become very dependent upon what FERC had to say about it. And if FERC were to have a policy that said actually we think that states, you know, declining or refusing to participate is just not acceptable, then you'd really squarely tee that up as kind of a conflict preemption issue, which I think in the Court's mind wasn't there and they viewed it as kind of a good thing that there was a cooperative federalism going on in the sense that FERC was saying, you know, we're willing to be somewhat accommodating to state policies in this respect.

But in a way it shows how all three of these cases kind of blur a little bit these field preemption and conflict preemption lines.

MR. MINZNER:

I think I agree that an important component of that decision is the recognition that the FERC Order setting out participation in the organized markets by Demand Response permit state opt out. And that is something the Court viewed as a favorable point in indicating the Commission had jurisdiction to issue these rules.

So you very much have this notion that in some sense there is some dynamism here about trying to figure out where FERC's jurisdiction is, is in part dependent on the structure of the rule and the relationship of the states in implementing it.

MS. KINDALL:

And to the extent there are clear lines in this world, wholesale would be FERC and retail would be the state. And so I think Erin has it exactly right. It's a conflict preemption analysis that would apply to the specifics of your horrible hypothetical.

(Laughter.)

MR. CAPLAN:

Well, thanks.

(Laughter.)

MR. CAPLAN:

Let me offer another. In *EPSA*, I think that the Court recognized that FERC was exercising its affecting jurisdiction. That is to say that inviting Demand Response into the wholesale market, and setting the terms and rates for that service, was not a direct jurisdictional act. It wasn't regulating a wholesale sale of electric energy. But it affected the wholesale sales of electric energy and the wholesale prices in the market.

Similarly, the Court found that that regulation did not constitute setting a retail rate for electric energy. The Supreme Court found that. So the Supreme Court didn't accept the D.C. Circuit majority—it was a two-one split—it didn't accept the D.C. Circuit majority view that demand response is in the retail market and therefore it's state jurisdictional, FERC, keep your hands off it.

Instead the Court found FERC was not regulating the retail rate of electric energy and therefore FERC did not cross the line. But meanwhile, in *Hughes* the Court could have said to Maryland and New Jersey, you're not setting the PJM Auction Clearing Price for Capacity, or the Day Ahead Clearing Price for energy. You've got a contract for differences that affects three generators in two states, but it doesn't set the Clearing Price, so you're not setting the wholesale rate.

But the Court didn't do that. The Court took, on the one hand in one case, a very narrow view of what it meant to set an electric rate at retail; and in the other case, a more expansive view of what it meant to set the wholesale price of Capacity or Energy.

So is this emblematic of a prejudice in favor of FERC jurisdiction when it's a jump ball, or a close call? Or am I reading too much into this?

MS. KINDALL:

Absolutely.  
(Laughter.)

MS. KINDALL:

Next question?  
(Laughter.)

MS. MURPHY:

I mean, one of the arguments that was made in the two cases that kind of harmonize on this issue, you know, I mean the language in the Federal Power Act dealing with FERC's jurisdiction says "for or in connection with wholesale rates." So anything received or in connection. And that "in connection with" language is quite broad, and I think is what kind of—and the Court highlighted that language in the *Hughes* case in kind of saying, you know, whether this is kind of directly setting, and whether it's setting in a narrow or a broad realm is a little beside the point because we have statutory text that says that.

Now we certainly made the argument in *EPSA* that Congress would have seemed to be preserving for states the same scope of authority over retail rates, meaning "for or in connection with" should apply there.

I think that probably the best reading of *EPSA* is that they at least implicitly didn't accept that there was a complete parallel in that sense as to what FERC's authority over wholesale rates is versus the states over retail. And I think in a sense before you even kind of get to the "affecting" jurisdiction, I think just in that kind of first instance question of the authority over the rate itself, I do think it's a little hard to reconcile the opinion if you were to accept the premise that the jurisdiction over the rate itself is the same in each context.

MR. MINZNER:

I mean, I think it's natural to try to seek some symmetry in the opinions from *Hughes* and *FERC v. EPSA* to try to say that, well, there's some necessary link between the tests governing federal jurisdiction and the tests governing state jurisdiction. But it's not obvious to me that that's right.

I mean the questions, the core legal questions in the cases stem from different sources. You know, *FERC v. EPSA* is a question about the Federal Power Act. FERC is an agency that has the power given to it under its organic statute. And so the question that comes up in *FERC v. EPSA* is what does the FPA mean? What does the NGA mean?

The question that comes up in *Hughes* is that it's a core Constitutional question. You know, what does the Supremacy Clause mean? What does, in some sense, the dormant Commerce Clause mean?

So if you view them as different questions in that sense, one is a Constitutional question about the limits on the states' powers. The other is a statutory question about what actually has been given to FERC. You know, there is no reason to think you wouldn't get different and asymmetric answers.

MR. CAPLAN:

You know, I think that in the *Learjet*, or *Oneok* case, one of the arguments that was raised in favor of preempting the states was that the Federal Power Act does *not* have an "affecting" clause for the states; that *it does* have an affecting clause for FERC. So FERC can regulate those matters affecting wholesale sales and rates.

And that was not sufficient for the majority in *Learjet*, and it ruled that states could regulate this area as well, even though it didn't get into a state-affecting clause. But in some ways I look at *EPSA*—and this is where you can have at it—but I look at *EPSA* as similar to *Learjet* in that the Court found FERC had jurisdiction over Demand Response even though Demand Response was not a sale or a resale of electric energy in interstate commerce, because Demand Response affected such sales and such prices.

At the same time, Demand Response affects retail rates. So is it similar to *Learjet*? And if so, if there were a challenge, then wouldn't that affirm that conflict preemption would apply to the challenge of the state activity in Demand Response, too?

MS. KINDALL:

I think clearly it would be a conflict preemption analysis. I actually think *EPSA* was decided on more practical grounds. I think, just that the impact on the wholesale markets nationwide with the elimination of Demand Response, I think that was really what was governing. And the fact that the states weighed in and said—they weren't there saying, protecting their jurisdiction saying oh, no, no, no, FERC can't be there. The states weighed in and said FERC absolutely should be able to do this, as well.

So I think that you can, you know, sort of slice and dice all the legal analyses, but I think at the bottom that's what really was going on.

MS. MURPHY:

We did have a few states on our side, too, but. . . (Laughter) but, no, I think that makes sense. I mean when you look at the way the Court was thinking about it, it was very much this kind of that this is happening in FERC's market, and how else can we make sure this happens in FERC's market if FERC can't control it? Which is a little bit divorced from kind of the starting principle of, well, wait, is it wholesale or retail? And what is really, you know, what is it affecting and what is it directly affecting? And it's kind of coming at it, I think that's right, from a much more practical lens in that respect.

MS. KINDALL:

Which was what, you know, drove Justice Scalia nuts. He's like, where's my lines? You know, where's my—you know, where's my nice clean lines? And I think that the majority was having a little more practical of an application.

MR. MINZNER:

You know, I think certainly one of the takeaways from the case is that there are a lot of things that the states can do that will have an impact on the federal rates, and there are a lot of things the Federal Government can do that will have some sort of an impact on the state rate. And you don't answer the question by simply asking: Is this going to lead to something different happening at the other level?

You know, I think it's pretty obvious, after *Learjet*, that the scope of state activities that might push around or have an impact on the federal rate is room for that. Similarly, the same thing, after *FERC v. EPSA*, that case recognizes that there is going to be some impact on the non-jurisdictional markets. And I think the Court indicates a comfort with that.

MS. KINDALL:

And I think *Hughes* really made a very good point about—in the lower levels of the *Hughes* case in the Third and Fourth Circuits, there was argument that anything at all that affected the FERC market would have to be preempted.

And, you know, the Third Circuit sort of set that aside, and the Supreme Court set that aside. And I thought that was a pretty valuable line for the Court to draw, to say, no, just because it affects the market doesn't preempt it. And that was a reassurance.

MS. MURPHY:

I think that's an interesting aspect of *Hughes*. Because the argument, you know, that there were a couple of different arguments advanced, and FERC was really the one that advanced more often the argument that it was preempted because it was within FERC's affecting jurisdiction.

And the Court didn't—I mean, one of the courts along the way really rejected that. I think the Supreme Court just kind of slid past that and didn't really feel the need to go there. But it certainly would have been—probably had a little more effect, you know, to have that, especially after an *EPSA* where you had the Court take the step of making a point of accepting the principle that it has to be directly affecting, which I'm not sure anything in the Opinion turned on that, but they felt the need, you know, they had the chance before them to clarify: We are going to say it has to be directly affecting to fall within Affecting jurisdiction, which is an important principle to have the Court, you know, have an opinion from the Court that says that at this point.

MS. KINDALL:

And, Max, we won't blame you. You weren't there, yet.  
(Laughter.)

MR. CAPLAN:

I read *Hughes* as really applying field preemption, not conflict preemption. It seemed that the Court explicitly declined to consider what the effects on the wholesale market were, which would have been necessary if the Court were applying conflict preemption. It didn't come right out and say that. And I think a number of us were speculating that the reason that the Court heard the Fourth Circuit case and not the parallel New Jersey Third Circuit case, was because the Fourth Circuit ruled on both conflict and field preemption.

And then the Court didn't exactly clarify the issue—it didn't at all—but I still read it as a field preemption case, since it declined to get into the nitty gritty of the impacts on the wholesale market.

What do you all think?

MS. MURPHY:

I think it's a little hard to tell. I think—I tend to agree, that it leans more toward field preemption. There's an interesting footnote in the Opinion that I actually think kind of pushes the furthest in the direction of field preemption, which is the footnote where the Court was saying it didn't matter that FERC had tried to accommodate this.

And they said, you know, whether or not FERC did accommodate it is irrelevant because the state was acting in FERC's sphere. And that is really classic field preemption language.

I mean, it doesn't, you know, say "field," but the footnote reads precisely like it doesn't matter if FERC could fix this, the point is it's FERC's to do and therefore the states can't do it at all.

Now at the same time, I think the opinion, you know, defines a pretty narrow field. I mean I don't think it's implying a principle of whenever you're dealing with a wholesale rate that is FERC's field and states have no business doing anything there. It seems to be a field that maybe is even kind of specifically the field of, you know, PJM can auction rates, and they're leaving for another day how far it goes beyond that. But it does seem to me to be more a field preemption approach.

MR. MINZNER:

I think it's a very hard question to answer because the Court didn't answer it for us, right? It doesn't seem like the Court was interested in speaking on whether this was a field or conflict preemption case. I do agree that there's some language pointing in the field direction.

In part I think it's a reflection of the test the Court adopted. You know, I grew up in a state that doesn't have an organized wholesale market. If it's a field preemption case, sort of what does this mean in the bilateral electric markets?

It would mean, I think it would be preempted for a state outside of an organized market to do something like this, but it's hard to even imagine what that would be, given that the contract and the preemption was so closely tied to the notion of an organized capacity market. So I think it's hard to even think about it in a field and conflict way, given that the test it gave us was so closely tied to the structure of the FERC organized market.

MR. CAPLAN:

Well before we turn it over to you in just a moment, I think in my simplistic way of looking at this, if I were getting a memo from a junior associate, I would want it to analyze what is the basis of jurisdiction? Is it direct? Or is it affecting? Because we heard that affecting has some implied limitations, and that's an important fact. And then if the state is acting in the same area, is the state acting under an area reserved for it under the Federal Power Act or the Natural Gas Act? Or is it merely acting under something that affects retail rates or retail services?

And then on the preemption front, I would ask: Does field preemption apply because Congress occupies the field completely? Or does conflict preemption apply?

It's amazing that we can read so many decisions and so many briefs and not be able to draw a nexus between the basis of jurisdiction and the form of preemption. But I would say that the reason we can't might be something that a Supreme Court advocate like Erin, or the General Counsel or the Attorney General could answer in terms of flexibility in politics. But to me that's what was wanting in these decisions, clarity squandered, which is good for the Energy Bar, unfortunately.

MS. KINDALL:

And, I would say, Stu did a very nice eleven-page set of materials that I think are part of the materials for here, and gave a wonderful little graph of, okay, now you have direct versus direct, and direct versus indirect, and where does this all fit? And where do you fill it in the chart?

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And it was a good analytical construct that I think had nothing to do with these decisions, but it was a good way to try to make some sense of these decisions.

And so I think that with *Hughes*, I think it was a direct versus direct. I think states had direct authority for generation, and FERC had direct authority for its markets. And I think in that direct clash FERC wins. And I think that to the extent there are those kinds of direct clashes, for the most part FERC wins. I think that *Learjet* is really the exception.

MR. CAPLAN:

Thank you. I think that *Learjet* would be two indirect forms of jurisdiction, and I think that if *EPSA* were a preemption case it would also. And I would expect in both that conflict preemption would apply.

So we've just filled out two boxes of a 2 x 2 grid of four boxes, but in any event it's just a simplistic way of looking at it, and certainly not the way the Court looked at it.

MS. MURPHY:

I thought it was helpful, though. Just to say, you know, a word in defense of the Court, I mean while I think it's frustrating for people who practice to not have this clear guidance from them on how to approach it, I mean I do think that their reluctance to provide it is animated by their decision that it's better to not give totally clear guidance than to kind of mess it all up in an area that they don't understand as well as all the people in this room do.

And, you know, I think that they want to make sure they fully appreciate the consequences of what they're going to say and how that's going to affect, you know, the next case, the broader energy markets, all of that. So while it is a little frustrating, you know, I mean I think there's a benefit to it all that maybe kind of nets out.

MR. CAPLAN:

That's a refreshing breath of humility imputed onto the Supreme Court.  
(Laughter.)

MR. CAPLAN:

So with that, why don't we turn it over to the audience for some questions that I'm sure you have for this esteemed panel. Is there a microphone that will traverse the room? Yes?

Just please state your name and then your question.

MR. BARTHOLOMEW:

It's Henry Bartholomew, EEI. I'm just curious, because you've painted a picture where on the one hand the states are trying to have more generation, and generation that would help contain rates for retail customers. On the other hand, the Commission is doing some activities certainly overseeing the organized markets, and with the DR and wholesale, looking for a similar end result.

So how—I'm curious, on the Commission side, you know we have with PJM all the rules put in place to try and get it right to let new generation in and not dissuade it, and keep prices down with DR.

So what's the path through this if the common goal is to try and keep retail rates relatively affordable and keep enough supply to meet demand in a very changing time with the Clean Power Plan, et cetera?

MS. KINDALL:

I think that the goal isn't necessarily to depress rates. I think the goal is to make sure that the citizens of the various states have reliable energy. And when you add the environmental overlay of clean and renewable energy as a valid state policy.

And I think the—and I won't speak for the Commission, but I think that for both the states and the Federal Government it's how do you best do that in a way that encourages investment, and to make sure that when people turn the lights on and it's ten degrees above zero, that they have both light and heat in their homes. So I think it's nothing more fundamental than that.

MR. MINZNER:

Yeah, again I can't speak for the Commission either. I mean I guess I would say that I would come back to the core statutory obligation under the Federal Power Act, not to keep rates high or low but to ensure that they are just and reasonable.

MR. CAPLAN:

If capacity or energy prices are suppressed through uneconomic entry, then you're not providing sufficient revenue. It's kind of like when an investor-owned utility that's vertically integrated and owns generation brings a plant online, it's entitled to a reasonable opportunity to recover its investment and a return on it, provided it was prudently made.

So there are analogies between the two. You can't have rates that are too low in either context or it's not fair for someone. But still I think there will be a lot of challenges coming ahead for how do you satisfy the demands of greenhouse gas reduction in a market that might not be sending the price signals.

If you contrast it to what happens if you have a cap-and-trade system, a nuclear power plant that's allegedly under-recovering from market revenue and might have to shut down, would receive a higher energy price if all of the energy bidders had to bid in the cost of emissions' allowances under a cap-and-trade system.

And then you'd have market signals that worked. But in the absence of such a program, if you start having state-by-state, because Clean Power Plan is state-by-state, subsidies, then you can run into trouble because you could be perverting the wholesale market in the process.

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And I'm sure that one day in the not-too-distant future, before we have effective cap-and-trade systems in place, the Commission will be asked to opine on that very issue because it will really affect investments that people make, assuming the risk that the market would be competitive, and not assuming the risk that the market would be subverted or impure due to subsidy.

MS. KINDALL:

Well, excuse me, but there's no state program that could possibly either pervert or subvert any federal market, I'm sure.

(Laughter.)

MR. CAPLAN:

Not in Connecticut, anyway.

(Laughter.)

MR. CAPLAN:

So do we have another question?

Yes, Carmen [Gentile].

AUDIENCE PARTICIPANT:

Would the *Hughes* case have come out differently if the subsidy to the generators were paid out of general state revenue, rather than a non-bypassable charge to the electric distribution companies?

MS. MURPHY:

I don't think so. I think actually that would have made it an even easier case, in my view, because it would have been more—you know, you wouldn't have even had the argument about this isn't being done kind of by the state, but I don't know if others disagree with that.

AUDIENCE PARTICIPANT:

May I ask a follow up? So what about a state that allows municipal generators within a state not to pay state taxes? Is that a violation of *Hughes*?

MS. KINDALL:

No, because the Supreme Court deliberately—expressly said that tax abatements and subsidies were okay. And the argument was made at the Supreme Court oral argument that all subsidies would be bad because it would affect the market.

And the Court pretty explicitly rejected that argument, thankfully. You know, whether it's tethered or not is another question, but I think it's pretty clear that direct tax subsidies over land, anything you wanted—anything the state wants to do that way is clearly permissible and fair game.

MR. CAPLAN:

Can you elaborate? I think the untethered part is really important in your answer.

MS. MURPHY:

I mean, to go back to your original question, I mean to me if everything were the same and the source of the money were just different, I don't think that would change the result.

I mean, if you took—if you changed some other factors and the money were coming from general, I don't think the fact that it's coming from general revenue, you know, necessarily makes it okay or necessarily makes it not okay. It's going to turn on how the program is structured and whether those revenues are tethered to clearing in the market.

MR. CAPLAN:

One last question, perhaps.

AUDIENCE PARTICIPANT:

If no one else has one, I would like to ask you if you could give us your forecast as to where you think the courts will go in this next ten years of litigation that you're predicting.

You said that these were narrow rulings, so in what direction will they go? And also what, in addition what you would forecast, what would you advocate? What, in your opinion, should the courts be doing? You mentioned *Hughes* restricted itself to preemption and not conflicts, but I'm wondering with FERC trying to have free market forces, for instance Max Minzner with your enforcement background, would you go after market manipulators who are private entities? Or are the states trying to manipulate the free market forces, and pick winners and losers? The contract-for differences is basically an insurance against failure to protect the market participant.

So I'd just like to know what—do you think the courts should be expanding and not restricting their interpretations? Or in which direction would they go? And maybe you have a different opinion.

MR. MINZNER:

Well, I mean I think it's very hard to predict the path of litigation. I do think it's inevitable. I think it's going to start out. Certainly one of the things I find striking about the three cases is that they each came up from a very different procedural posture.

So one of course is *Learjet* which suggests that we're going to see litigation in state courts. And that will be one way that this will get sorted out. Obviously *FERC v. EPSA* came up, very traditionally for a FERC Order on appeal through the D.C. Circuit. That's one path of litigation, rulemakings, 205, 206 filings at FERC. And then of course *Hughes* itself came up through the Federal District Courts. All three of those are going to be areas in which this gets sorted out. So I think that means you've got three different procedural pathways by which we're going to see these cases get interpreted.

MS. KINDALL:

I agree.

MS. MURPHY:

I'm not sure it's such a bad thing right now for courts to be a little cautious and a little case-by-case. I mean, some of this is a product of, you know, this is an area that, while it may not seem like it changed yesterday to people who practice in this area all the time. I mean, by the way courts think about things, you know, it takes a decade of a market changing to really tee up a lot of these legal challenges. And I think that's why you are seeing these things kind of reaching the Supreme Court now. It's in a sense a product of changes that have been going on in a marketplace that's where the states and federal—and there's more room for tension I think than there's ever been in the way the markets work right now.

And when you've got that kind of practical dynamic going on, you know, maybe it's not the worst thing in the world for courts to kind of think about it as, well, we'd like to have bright-line rules but we need to make sure we understand what their consequences are now that we have a market that looks a little bit different from what Congress was thinking about when it passed the Federal Power Act almost a century ago.

So I think we may see, especially with courts taking their cue from how the Supreme Court has done this, that we might see a little bit more of that kind of: we're going to look at each case just kind of as it comes to us, and not try to announce broader principles unless we have to.

MS. KINDALL:

I think this is just a wonderful time to be in energy law. I think there is an awful lot of dynamic forces going on right now. And we all need to remember what is at the bare basics of why we do this. You know, every family, every person here in the entire country wants to turn on their lights, wants to heat their homes, wants to drink clean water, wants telecommunications. And how those services of heat, light, water, are going to be delivered in the next twenty years is changing.

And I think that as practitioners all of you are going to have an impact on that, and I think that's really something to keep in mind; that, you know, that's what makes it fun. It is dynamic. And so I completely agree with both Erin and Max that it's going to be an era where you don't want such bright-line rules as to stop what is going to be inevitable innovation. And I think that really is going to make it a lot of fun for all of us.

MR. CAPLAN:

Well said. On that, we have run out of time. But I would like you to join me in showing appreciation for this fine panel. (Applause.)