NOS. 18-868, 18-879

In the Supreme Court of the United States

ELECTRIC POWER SUPPLY ASSOCIATION, NRG ENERGY, INC., AND CALPINE CORP.,
Petitioners,
v.

ANTHONY STAR, in his official capacity as Director of the Illinois Power Agency, *et al.*,
Respondents.

ELECTRIC POWER SUPPLY ASSOCIATION AND NRG ENERGY, INC.,
Petitioners,
v.

JOHN B. RHODES, in his official capacity as chair of the New York Public Service Commission, *et al.*,
Respondents.

On Petitions for Writ of Certiorari to the United States Courts of Appeals for the Seventh Circuit and Second Circuit

BRIEF OF *AMICUS CURIAE* MONITORING ANALYTICS, LLC, ACTING IN ITS CAPACITY AS THE INDEPENDENT MARKET MONITOR FOR PJM, IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether the FPA preempts only state subsidies that explicitly require a wholesale generator to sell its output in FERC approved auctions, or whether the FPA also preempts state subsidies that lack such an express requirement but that, by design, subsidize only generators that sell their output via such auctions, thereby achieving the same effect.

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INTEREST OF *AMICUS CURIAE*[1]

Monitoring Analytics, LLC, serves as the Independent Market Monitor for PJM ("Market Monitor"), and appears here solely in its capacity as the Market Monitor.[2]

Consistent with its unique role, the Market Monitor here seeks to protect and promote the public interest in and federal policy for competition-based regulation. The organized wholesale electricity market at issue in this case is operated by PJM Interconnection, L.L.C., which has been approved as a Regional Transmission Organization ("RTO") by the FERC.[3] Consistent with its competition-based regulatory initiative, FERC requires an RTO to operate a centralized wholesale electricity market independently from market participants. FERC requires RTOs to have a Market

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[1] In accordance with U.S. Sup. Ct. Rule 37.2(a), 28 U.S.C.A., all parties received timely notice of the filing of this brief and have provided consent to the filing of amicus curiae briefs, either by filing blanket consent letters that the Clerk of the Court has noted on the docket, or by providing their consent to amici. Pursuant to U.S. Sup. Ct. Rule 37.6, 28 U.S.C.A., Monitoring Analytics, LLC states the following: (1) Monitoring Analytics, LLC counsel authored this brief; (2) no counsel for a party to the decision below, or other entity, authored this brief in whole or in part; and (3) no person or entity other than Monitoring Analytics, LLC made a financial contribution to the preparation or submission of this brief.

[2] Monitoring Analytics, LLC, is solely owned by Dr. Joseph E. Bowring. Dr. Bowring is the President of Monitoring Analytics and the Independent Market Monitor for PJM.

[3] *See PJM Interconnection, L.L.C., et al.*, 96 FERC § 61,061 (2001).

Monitor that is independent from market participants and from the RTO.[4]

The core functions of the Market Monitor are to evaluate and review proposed market rules, tariff provisions and market design elements; review and report on the performance of the wholesale markets; and identify and notify the FERC of participant or RTO behavior that requires investigation.[5]

The Market Monitor is charged to protect the public interest in competitive wholesale electricity markets.[6] The Market Monitor's purpose is to promote efficient wholesale markets and to help realize the FERC's goal to regulate electricity markets through competition.[7] A priority concern of the Market Monitor is to detect, deter and prevent the exercise of market power in PJM markets.[8]

The Market Monitor is subject to a strict code of ethics prohibiting conflicts of interest or engagements with market participants and others that could interfere with the Market Monitor's independence and objectivity.[9]

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[4] *See* 18 C.F.R. § 35.34(k)(6).

[5] *See* 18 C.F.R. § 35.28(g)(3)(ii).

[6] *See* PJM Open-Access Transmission Tariff ("OATT") Attachment M (14-614 Pet. Ap. 78a); *see also*, 18 C.F.R § 35.28(g).

[7] *Id*.

[8] *Id*.

[9] *See* OATT Attachment M § XI; *see also*, 18 C.F.R § 35.28(g)(3)(vi).

SUMMARY OF ARGUMENT

The lower courts fail to properly apply recent and directly applicable precedent, the Supreme Court's decision in *Hughes v. Talen Energy Marketing, LLC*, 136 S. Ct. 1288 (2016). The issues presented are the same, and the legal outcome should be consistent. The lower courts elevate form over substance, converting *Hughes* from a substantive test into a semantic touchstone. As a consequence, if the law of preemption is not properly upheld, a major federal program to regulate wholesale power markets through competition and provide lower cost power to consumers will eventually fail, contradicting the regulatory scheme established by Congress under the Federal Power Act and harming the public interest.

ARGUMENT

A. Petitioners Correctly Argue that Substance Should Prevail Over Form and Explain the Importance of this Case.

Unlike Petitioners, Market Monitor does not directly participate in wholesale power markets. The Market Monitor's interest is to protect the PJM market design so that the underlying federal policy succeeds and serves the public interest.

The Market Monitor agrees with Petitioners' identification and explanation of the core error of the lower courts' decisions: a reading that "exalts form over substance."[10] The decisions entirely rely on a misreading of *Hughes v. Talen Energy Marketing, LLC*,

[10] Pet. at 20–21 (Cites to Pet. refer to the petition filed in Case No.18-868).

136 S. Ct. 1288 (2016), to prohibit only an explicit displacement of federal jurisdiction over federal wholesale ratemaking. Such a reading "effectively confines *Hughes* to its facts."[11] Legislators can easily contravene FERC's authority over wholesale rates by artful description or avoiding description of the mechanism rather than transparent statutory language. An explicit tether like that appearing in *Hughes* is easily avoidable, as the ZECs programs at issue here illustrate. Under lower courts' suppressive reading of *Hughes*, Maryland could have proceeded with its programs after a few tweaks to the wording. The issue here is whether *Hughes* stands for a principle or is limited to semantics. The law of preemption properly concerns more than proper wordsmithing.

If *Hughes*' proper and reasonable demarcation of federal and state jurisdiction over the nation's interconnected wholesale power market is not confirmed, it will mean the end of a major federal regulatory initiative.[12] It may effectively end federal control over the interstate wholesale power markets, contrary to the jurisdictional framework in the Federal Power Act. The record shows that FERC has gone out its way to accommodate the states. How have the states accommodated FERC? If anything, Petitioners understate the risk. The public will be ill served if regulation through competition survives in name only. There is an important public interest in uniform regulation of the bulk power grid.

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[11] *Id*.

[12] *See* Pet. at 30–31.

For over two decades, FERC has successfully worked to replace the obsolete cost of service ratemaking approach with a new regulatory approach based on competition and markets. FERC has made particular progress in the areas administered by organized markets, including the markets affected by the cases now before this Court: New York Independent System Operator, Inc. (NYISO); PJM Interconnection, L.L.C. (PJM); and Midcontinent Independent System Operator, Inc. (MISO). In PJM, after ongoing improvements over almost 20 years of effort, a framework of rules is in place that has demonstrated that it works to support sustained competitive investment and retirements. This is a remarkable achievement, even if FERC's goals are not yet fully realized. Competitive investment continues to compete with limited levels of state subsidized investment.

The current market design is manageable and has prospects for improvement. State subsidies for favored resources like the ZEC program at issue here go beyond what can be successfully accommodated. Subsidies are contagious. Subsidies for one uneconomic resource suppress prices for others leading to more requests for subsidies. Left unrestrained, state subsidies will eventually supplant FERC's competition based regulatory model.

The lower courts find that ZEC subsidies are indistinguishable from other programs that support renewables, known as Renewable Portfolio Standards (RPS).[13] This rationale is not a sound basis to find that ZECs are not preempted. The Supreme Court did not

[13] Pet. App. at 24a–25a.

hold that some or all RPS programs are exempt under its decision in *Hughes*. More importantly, RPS and ZECs are distinguishable and have material differences. RPS do not target or disregard federal rates. RPS programs require retail consumers to purchase a defined proportion of their power from renewable sources. RPS programs rely on Renewable Energy Credits (RECs) as a mechanism to demonstrate the quota is met. RPS programs impact wholesale markets, but indirectly. RPS quotas, operating through the RPS, have an important impact on wholesale prices, but this is incidental to states' meeting their procurement quotas.

New York and Illinois could tax carbon emissions directly. Illinois could have, like New York, joined a multistate carbon emissions market program. New York can seek a tighter emissions cap in its program. New York and Illinois instead opted for a new and different model. ZECs are not tradeable instruments linked to a quota for retail power purchases from zero emissions resources. ZECs are instead linked to the support of specific, existing, uneconomic units based on a mature technology, identified by state legislatures because competitive markets have resulted in lower net revenues to those units. ZECs programs tether the level of subsidy to prevailing wholesale price levels. That their purpose is to disregard wholesale prices can be unambiguously inferred from how ZECs programs operate. ZECs operate to confer benefits to particular assets based explicitly on lower than desired net revenues from competitive wholesale power markets. In the Illinois case, there is a specific target level of market revenue which, if reached, terminates the ZEC payments.

The proper constitutional analysis should evaluate ZECs based on what they do, not the rhetoric under which they are promoted. That is the essence of *Hughes'* holding that states are preempted from targeting or disregarding wholesale rates.[14] That states were "targeting" wholesale pricing was a driving principle applied in *Hughes*, in addition to "tethering."[15] Targeting or "disregarding" a wholesale rate is forbidden under *Hughes* without regard to whether the state's jurisdictional basis is valid.[16]

The issue is whether states can require customers to subsidize favored resources and thereby change the wholesale rate received by such resources. The lower courts do not separately consider the more substantial targeting and disregarding test, but instead improperly

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[14] *Hughes* includes two standards, (i) the targeting and disregarding test and (ii) the tethering test. *See Hughes* at 1298–1299. The Market Monitor emphasizes the former test in its argument here, but the New York and Illinois programs also show prohibited tethering. The language in the New York and Illinois programs is more nuanced than in Maryland's.

[15] *See Hughes* at 1298 ("That Maryland was attempting to encourage construction of new in-state generation does not save its program. States, of course, may regulate within the domain Congress assigned to them even when their laws incidentally affect areas within FERC's domain. *See Oneok, Inc. v. Learjet, Inc.*, 575 U. S. ___, ___, 135 S. Ct. 1591, 191 L. Ed. 2d 511, 528 (2015) (whether the *Natural Gas Act (NGA)* preempts a particular state law turns on "the *target* at which the state law *aims*" [emphasis in original]).[footnote omitted] But States may not seek to achieve ends, *however legitimate*, through regulatory means that intrude on FERC's authority over interstate wholesale rates, as Maryland has done here." [emphasis added]).

[16] *See id.* at 1299 ("We reject Maryland's program only because it disregards an interstate wholesale rate required by FERC.").

conflate it with the more superficial tethering test. As a result, *Hughes'* key criterion forbidding targeting or disregarding federal wholesale rates is misinterpreted and ignored. The substance of the law of preemption set forth in *Hughes* should be controlling.

B. The Uncertain Prospects for MOPR Reform Demonstrates Why the Law of Preemption Must Be Enforced.

The consequences of the failure to properly apply the law of preemption are evident in the current state of the latest in the series of proceedings for reform of PJM's market power mitigation rule in the capacity market, known as the Minimum Offer Price Rule (MOPR).

The MOPR is a form of market power mitigation and mechanism to ensure competitive market behavior in PJM's capacity market.[17] The wholesale capacity markets operated by PJM have endemic structural market power.[18] Market power mitigation rules are a necessary and permanent feature of such markets to ensure competitive outcomes. Mitigation means that offers and therefore prices reflect the fundamentals of supply and demand even when the behavioral incentives needed to create those outcomes do not exist naturally. Mitigation protects efficient market pricing by requiring competitive offers from those that would uncompetitively increase prices and from those that

[17] For the Court's earlier synopsis of the MOPR, *see Hughes* at 1294.

[18] The existence of *structural* market power means that offers that are not competitive interfere with economic price formation and market efficiency regardless of motive.

would uncompetitively decrease prices. Application of the MOPR requires calculation of competitive offers that ignore out of market subsidies.

FERC has determined that PJM's tariff is unjust and unreasonable unless the MOPR is reformed to "address subsidies to existing resources."[19] FERC knows what is required to ensure competitive markets.[20]

The lower courts relied upon FERC's statement that it could address the threat posed by state subsidies such as ZECs:

> If the Illinois program, in fact, impairs the functioning of the wholesale markets subject to FERC jurisdiction, the Commission thus has the means and the authority to confront those effects. The Commission is now considering the impacts on wholesale markets of these sorts of programs. Once it issues a final order in the above-noted administrative proceeding, any aggrieved parties will have the opportunity to seek judicial review. *See* 16 U.S.C. § 825l. At that time, a court of appeals can resolve any claims properly preserved for judicial review, such as the Commission's analysis of the effect of the Illinois program on federally-regulated wholesale markets or whether the Commission

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[19] *See Calpine Corp., et al. v. PJM*, 163 FERC ¶ 61,236 at P 154 (June 29, 2018) ("MOPR Order").

[20] The reform is about expanding the MOPR to cover existing resources in addition to new resources. *See* Pet. at 32–34.

impermissibly encroached on an area reserved for the States.[21]

FERC claims that it can confront effects of the ZECs program that impair the functioning of the wholesale market. FERC represents its priority concern as its anticipated future defense of MOPR reform against future state objections that such measures would encroach on state authority. At the time of the briefing, FERC had not yet determined "whether the PJM minimum offer price rule requires correction to address state initiatives such as the Illinois ZEC program."[22] Three weeks later, FERC determined that the PJM MOPR needs correction.[23] Six months further on there is no decision on a solution.

The implied premise in FERC's statement to the lower courts is that preemption analysis should turn on whether the federal agency can take steps to prevent state policies from conflicting with federal policies. Such potential preventive measures are irrelevant to such analysis. Application of the law of preemption does not turn on whether the federal agency believes it is necessary to or desires to show comity to a state's authority. The information properly relevant to the lower courts' analysis is whether the "Illinois program, in fact, impairs the functioning of the wholesale markets subject to FERC jurisdiction," not whether

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[21] Brief for the United States and the Federal Energy Regulatory Commission as Amici Curiae in Support if Defendants-Respondents and Affirmance, *Elec. Power Supply Ass'n v. Star*, Nos. 17-2433 and 17-2445 (May 29, 2018) at 8.

[22] *See id.* at 6.

[23] *See* MOPR Order at P 154.

FERC has "means and the authority to confront those effects."[24]

Requiring an agency to continually defend its authority prevents effective decision making concerning matters that are technically complicated and vulnerable to interference from special interests. Consumer access to wholesale power on economic terms is a vital public interest. An unprotected market rules structure in an industry characterized by market power can easily and subtly be diverted from serving economic goals promoting the public interest to self serving ones. Preemption doctrine promotes clear jurisdictional boundaries when properly applied and thereby serves the public interest in effective governance.

The ongoing story of the MOPR for protecting PJM markets demonstrates why the Court's refusal to require such measures as a prerequisite for the enforcement of preemption law is as wise as a matter of policy as it is correct as a matter of law. The MOPR has been continually litigated since the capacity

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[24] *See Hughes* at 1298 n.11 ("Maryland's program, Maryland and CPV assert, is consistent with federal law because FERC has accommodated the program by eliminating the MOPR's state-supported generation exception. Even assuming that this change has prevented Maryland's program from distorting the auction's price signals, however—a point the parties dispute—Maryland cannot regulate in a domain Congress assigned to FERC and then require FERC to accommodate Maryland's intrusion," citing *Northwest Central Pipeline Corp. v. State Corporation Comm'n of Kan.*, 489 U.S. 493, 518 (1989) ("The *NGA* does not require FERC to regulate around a state rule the only purpose of which is to influence purchasing decisions of interstate pipelines, however that rule is labeled.").

market it protects was put in place over ten years ago.[25] MOPR reforms have barely kept pace with the latest stratagems to circumvent the rule. The most recent such stratagem is ZECs. FERC has now made a formal determination that state subsidies programs (specifically including the Illinois ZEC program) are suppressing PJM wholesale prices to a point where prices are unjust and unreasonable under the Federal Power Act.[26]

FERC has formally determined that ZECs implicate FERC's core mission.[27] FERC knows what remains to

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[25] *See* FERC Docket Nos. ER05-1410, ER11-2875, ER13-535, EL16-49 and ER18-1314.

[26] *See* MOPR Order at PP 149, 151 ("The records in both cases demonstrate that states have provided or required meaningful out-of-market support to resources in the current PJM capacity market, and that such support is projected to increase substantially in the future. These subsidies allow resources to suppress capacity market clearing prices, rendering the rate unjust and unreasonable."); *id* at P 156 ("We are compelled by the evidence presented by PJM, Calpine, and other parties to these consolidated proceedings to conclude that out-of-market payments by certain PJM states have reached a level sufficient to significantly impact the capacity market clearing prices and the integrity of the resulting price signals on which investors and consumers rely to guide the orderly entry and exit of capacity resources. We cannot rely on such a construct to harness competitive market forces and produce just and reasonable rates. The PJM Tariff, therefore, is unjust and unreasonable.")

[27] *See* MOPR Order (FERC Commissioner Powell Concurring) ("Let me be clear: there is a problem. The Federal Power Act compels this Commission to ensure just and reasonable rates. The record before us clearly indicates that unfettered access to wholesale energy markets by state-supported resources leads to unjust and unreasonable rates. If the Commission did not find today that the

be done.[28] But FERC also knows that expanding the MOPR means forcing states to live with the costs that result from their choices.[29]

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existing PJM tariff is unjust and unreasonable, it would be ignoring the duties prescribed to it under the Federal Power Act.").

[28] *See* MOPR Order at P 153 ("[T]here is an important difference between a resource that offers low as a result of competition in the market and one that offers low because a state subsidy gives it the luxury of doing so. The state subsidy protects the latter resource from the potential downside of that bidding behavior. Thus, we find here that the increase in programs providing out-of-market support, such as ZEC programs, has changed the circumstances in PJM, such that it is no longer possible to distinguish the treatment of new and existing resources in the context of PJM's MOPR.").

[29] *See* MOPR Order at P 159 ("We recognize that, if PJM's MOPR applies to state subsidized resources with few or no exceptions, and yet the states continue to support those resources, some ratepayers may be obligated to pay for capacity both through the state programs providing out-of-market support and through the capacity market. The courts have directly addressed this point, holding that states "are free to make their own decisions regarding how to satisfy their capacity needs, but they 'will appropriately bear the costs of [those] decision[s],' … including possibly having to pay twice for capacity."[291: *Id*. at 97 (citing Connecticut PUC, 569 F.3d at 481).] Nonetheless, we do not take this concern—or the states' right to pursue valid policy goals—lightly. Which brings us to the second aspect of our proposed replacement rate.

In addition to expanding PJM's MOPR, we also preliminarily find that it may be just and reasonable to accommodate resources that receive out-of-market support, and mitigate or avoid the potential for double payment and over procurement, by implementing a resource-specific FRR Alternative option. We therefore propose that PJM adapt its current FRR option to allow, on a resource-specific basis, resources receiving out-of-market support to choose to be removed from the PJM capacity market, along with a commensurate amount of load, for some period of time.").

Excluding state subsidized projects from consideration in wholesale supply, assuming states actually move forward with such subsidy programs, results in surplus generation capacity. FERC is concerned to avoid this waste even though state policies create it and states could still pursue their objectives through other means. The essence of the states' position is that FERC should prevent waste attributable to such states' policies by abdicating federal regulation of the wholesale market.

States have no valid complaint against an effective demarcation of the federal/state jurisdictional divide.

States reveal their intent to intrude upon federal prerogatives and change its priorities when they oppose an effective MOPR on the grounds that it creates wasteful excess capacity.[30]

That no program can both accommodate state subsidized supply and protect federal jurisdiction over wholesale pricing is inconvenient but fundamental economic logic. That FERC finds it difficult to protect its authority and to accommodate states' policies

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[30] *See* Protest and Comments of the Maryland Public Service Commission, Docket No. ER18-1314-000 May 7, 2018 at ("… [R]esources with attributes important to meeting state policies may not clear the market. As such, customers may still need to buy capacity in the BRA, in addition to procuring resources with attributes they value, essentially buying more capacity than needed."); Protest of the New York State Public Service Commission and New York State Energy Research and Development Authority, ER18-1314-000 (May 7, 2018) ("… [T]he MOPR-Ex would expand existing mitigation measures in a way that inappropriately would impede the states' ability to pursue legitimate energy and environmental policy objectives.").

without harming the public interest demonstrates why the law of preemption is needed and must be applied here. If the state subsidy programs are preempted, the harm is avoided. Proper application of the law of preemption will preserve the jurisdictional boundaries set forth in the Federal Power Act, and having those boundaries properly set will encourage better policy choices and better federal/state coordination of policy choices. The law of preemption should be upheld.

CONCLUSION

Accordingly, the Market Monitor respectfully urges that the holding of the United States Courts of Appeals for the Second and Seventh Circuit be reversed.

Respectfully submitted,

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