No. 18-879

IN THE

Supreme Court of the United States

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, GREGG C. SAYRE, in his official capacity as Chair of the New York Public Service Commission, DIANE X. BURMAN, in her official capacity as Commissioner of the New York Public Service Commission, JAMES S. ALESI, in his official capacity as Commissioner of the New York Public Service Commission, and EXELON CORP., R.E. GINNA NUCLEAR POWER PLANT LLC, CONSTELLATION ENERGY NUCLEAR GROUP, LLC, NINE MILE POINT NUCLEAR STATION LLC,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

Reply Brief for Petitioners

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REPLY BRIEF OF PETITIONERS

The Question Presented in this case is how the reasoning of *Hughes v. Talen Energy Marketing, LLC*, 136 S. Ct. 1288 (2016), applies to a state subsidy program that is designed to deliver exactly what the program preempted in *Hughes* delivered—a state-determined, above-market payment for each megawatt-hour of electricity that favored producers sell at wholesale—without a formal "bid-and-clear" requirement. Had New York enacted the ZEC subsidy program in its current form and merely added an explicit requirement that subsidy recipients sell their output at wholesale, it would be preempted under *Hughes*. Respondents nevertheless claim that *Hughes* requires preemption *only* when a formal "bid-and-clear" requirement is present—that *Hughes* should be "limited" to its facts. E.g., Brief in Opposition of Respondent Exelon Corporation ("Ex. Opp.") at 2; Brief in Opposition of New York State Respondents ("NY Opp.") at 3. But the bid-and-clear requirement made *Hughes* an easy case. This Court left for another day the question of how to mark the boundary of exclusive federal authority over the payments producers receive in connection with wholesale sales. 136 S. Ct. at 1293.

Due to States' efforts to skirt *Hughes*, that day has arrived. The court of appeals conceded that the ZEC program came "as near as can be without crossing" the line that demarks exclusive federal authority over wholesale rates, Pet. App. 22a, but only because the court read *Hughes* as drawing that line at a bid-and-clear requirement. Thus, the court dismissed as irrelevant the practical reality central to a proper preemption analysis: Petitioners' well-pleaded allegation that New York's ZEC program did not need a formal bid-and-clear requirement to function as a direct wholesale subsidy because the favored nuclear producers necessarily sell all of their output at wholesale—*i.e.*, they always "clear" in wholesale markets 100% of the electricity they produce. Given how easy it is for States to design around a formal bid-and-clear requirement, limiting *Hughes* to that unique circumstance effectively renders it a dead letter.

Although Respondents pretend otherwise, the decision below and the comparable ruling of the Seventh Circuit in *Electric Power Supply Association v. Star*, 904 F.3d 518 (7th Cir. 2018), have caused considerable concern. This Court has the benefit of numerous *amicus* briefs from industry participants and expert economists who believe these rulings seriously compromise the longstanding federal policy favoring market-based wholesale rates. The neutral and independent market monitor for the PJM market ("Market Monitor")—the world's largest wholesale energy market, covering 13 states and the District of Columbia—agrees. See Amicus Brief of Monitoring Analytics, LLC ("Monitor Br."), at 4, (Feb. 7, 2019) ("If anything, Petitioners understate the risk. The public will be ill served if regulation through competition survives in name only.").

The Federal Energy Regulatory Commission (FERC) has acknowledged that ZEC programs distort wholesale markets, and is struggling to find a way to limit the damage. See *Calpine Corp. v. PJM Interconnection, LLC*, 163 FERC ¶ 61,236 at 68–69 (out-of-market support for certain generators, such as ZEC programs, "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," such that FERC can no longer "harness competitive market forces [to] produce just and reasonable rates"). While FERC has inexplicably concluded that *Hughes* requires it to tolerate these distortions, *Hughes* holds the opposite: States "cannot regulate in a domain Congress assigned to FERC and then require FERC to accommodate [that] intrusion." 136 S. Ct. at 1298 n.11.

Only this Court can provide the definitive guidance that FERC, the States, and industry participants urgently need. Emboldened by the decisions now before this Court, States are moving aggressively to increase the wholesale revenues of favored producers above the level FERC has deemed just and reasonable. And FERC's apparent acquiescence suggests a fundamental shift away from the longstanding federal policy of requiring that wholesale rates be set through competition, without anything approaching the formal process or reasoned decision-making that should accompany such a dramatic change. As the Market Monitor put it: "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." Monitor Br. 4. The Court should grant the Petition.

I. That Two Circuits and FERC Misread *Hughes* Counsels in Favor of Review

Like the respondents in *Hughes*, Brief in Opposition at 15–31, Nos. 14-614, 14-623 (Feb. 11, 2015), Respondents argue that review is not warranted because there is no circuit split, Ex. Opp. 12–18; NY Opp. 15–17. Petitioners did not seek review on that basis, but rather because, as the Court recognized in *Hughes*, whether States can subsidize wholesale electricity sales in the manner of New York's ZEC program is a question of considerable importance to the energy industry and the Nation's economy. The courts of appeals in this case and in *Star* approved such programs based on an incorrect reading of *Hughes*. Only this Court can clarify the scope of its ruling. Those are plainly grounds for review by this Court. See Sup. Ct. Rule 10(c).

If Respondents want to count noses, see Ex. Opp. 1, 12 ("all eight judges to have considered the question agree"), they cannot overlook that this Court unanimously held in *Hughes* that States cannot supplant FERC-authorized "rates and charges … received … for or in connection with interstate wholesale sales" by guaranteeing favored producers will receive an alternative, state-determined level of compensation over and above those amounts. 136 S. Ct. at 1298–99 (citing § 824d(a)). As explained in the Petition and confirmed by *amici*, that is precisely what the challenged subsidy does: ZECs guarantee that uneconomic nuclear generators receive a minimum, state-determined level of compensation in connection with wholesale sales, regardless of FERC-approved market-based rates. See Pet. 18–23; Amicus Brief of Energy Economists ("Econ. Br."), at 10–13, (Feb. 7, 2019).

If anything, that two courts of appeals have confined *Hughes* to its facts counsels in favor of review. See *Thurston Motor Lines, Inc. v. Jordan K. Rand,* *Ltd.*, 460 U.S. 533, 535 (1983) (lower courts should not "confuse[] the factual contours of [this Court's decision] for its unmistakable holding"). The lower courts' reading gives States a roadmap for circumventing *Hughes*: "Legislators can easily contravene FERC's authority over wholesale rates by artful description or avoiding description of the [subsidy] mechanism…. An explicit tether like that appearing in *Hughes* is easily avoidable." Monitor Br. 4.

Nor should the Court deny review in deference to a cursory *amicus* filing by FERC and the United States in *Star*. That brief reflects a sharp and unexplained departure from the well-established federal policy that market-based methods should determine just and reasonable wholesale electricity rates.[1] Moreover, this Court must independently determine whether the State has overrun the jurisdictional boundary Congress established in the FPA. Pet. 32–33 (citing *New York v. FERC*, 535 U.S. 1, 41–42 (2002) (Thomas, J., dissenting)). This Court has rejected FERC's preemption position before, see *Pac. Gas & Elec. Co. v. State Energy Res. Conservation & Dev. Comm'n*,

[1] Exelon implies that the views FERC expressed in this *amicus* brief are entitled to *Chevron* deference. Ex. Opp. 4, 32 & n.9. Even if FERC's jurisdiction-defining statutory provisions were sufficiently ambiguous to justify *Chevron* deference, but see *FERC v. Electric Power Supply Ass'n*, 136 S. Ct. 760, 773 n.5 (2016), it is doubtful the agency's litigation position in *Star* is entitled to deference given its views in *Hughes*, see Pet. 32, and its longstanding market-based approach to wholesale rate-setting, see Amicus Brief of Am. Petroleum Inst. and Nat. Gas Supply Ass'n in Support of Certiorari ("API-NGSA Br."), at 7–17, (Feb. 8, 2019). See *Auer v. Robbins*, 519 U.S. 452, 462 (1997); *Good Samaritan Hosp. v. Shalala*, 508 U.S. 402, 417 (1993); *Christensen v. Harris Cty.*, 529 U.S. 576, 587 (2000).

461 U.S. 190, 222–23 (1983), and should do so again here.

II. The Threat the ZEC Program Poses to the Proper Allocation of Authority Under the FPA Warrants This Court's Intervention

The gravamen of the Petition is that the ZEC program fundamentally shifts the FPA's division of federal and state authority and threatens the integrity of a major federal energy policy. Numerous *amici* agree. Monitor Br. 3–5; Econ. Br. 14–19; API-NGSA Br. 5–17; Amicus Brief of Industrial Customers, at 5–13 (Feb. 8, 2019). Rather than responding to these pressing policy concerns, Respondents urge the Court not to worry about the downstream effects of ZEC subsidies on market supply and prices. See NY Opp. 18–23; Ex. Opp. 19–21. These arguments are misplaced.

1. The New York Respondents argue that "state regulation of production … is not preempted merely because it affects conditions in the federal field." NY Opp. 18–21. This is a straw man. New York's ZEC program does not merely have "spillover" effects on wholesale markets. *Id.* 18. In both design and operation, ZEC subsidies impermissibly supplant FERC-authorized rates by guaranteeing favored producers will receive state-determined levels of income when making wholesale sales. See Pet. 18–23. The constitutional infirmity of ZECs stems not from the indirect *ex post* market effects of promoting energy production, but from New York's *ex ante* "second-guess[ing] the reasonableness of interstate wholesale rates" and "disregarding" those rates in favor of wholesale compensation levels the state

prefers. *Hughes*, 136 S. Ct. at 1298–99. That is the core holding of *Hughes*, which Respondents and the lower courts have ignored. Pet. 18–27.

2. Similarly inapt is Respondents' claim that other state renewable energy programs, such as renewable energy credits ("RECs"), produce similar market effects. NY Opp. 21–23; Ex. Opp. 21. The preemption inquiry does not turn on the downstream impacts of these programs; what matters is whether such programs impermissibly second-guess or disregard FERC-authorized rates.[2] The two programs are materially different in that way. Although ZECs are available only to failing nuclear plants, RECs are available to all qualified renewable generators, regardless of economic need. And ZEC prices are set at state-determined rates that move in tandem with wholesale prices, whereas RECs are traded on the free market. See Pet. 10 n.1; Monitor Br. 5–6. ZECs aim to remedy perceived insufficient wholesale market rates (forbidden under *Hughes*), while RECs do not.

3. Respondents also argue that FERC is best suited to remedy the market distortions that of ZECs cause. NY Opp. 20–21; Ex. Opp. 19–20. This argument is misguided for three reasons.

First, the premise of this argument is that if FERC can mitigate the harmful impact of ZECs on federal energy policy, ZECs are not preempted. That is exactly backwards. See *Hughes*, 136 S. Ct. at 1298 n.11; *Nw. Central Pipeline Corp. v. State Corp.*

[2] *WSPP Inc.*, 139 FERC ¶ 61,061 (2012), predates *Hughes* and thus did not consider this question.

Comm'n of Kan., 489 U.S. 493, 518 (1989) ("The NGA does not require FERC to regulate around a state rule.").

Second, as the Market Monitor comprehensively explains, FERC'S ability effectively to ameliorate the market impacts of ZECs is doubtful. Monitor Br. 8–15. After years of consideration, FERC is not close to acting to reduce the damage to wholesale markets that these programs produce—and in the meantime, wholesale rates are distorted by multi-billion-dollar subsidies flowing to favored producers.

Third, FERC has already determined that ZECs are causing serious distortions in the wholesale markets. See *Calpine*, 163 FERC ¶ 61,236, at 63–69. Those real world impacts strongly suggest the lower courts have drawn the jurisdictional boundary incorrectly, a question not likely to be ventilated further in FERC's regulatory efforts. By the same token, Petitioners cannot vindicate the jurisdictional claim they press here by seeking judicial review of any remedial order FERC might adopt in the future.

III. The Decisions Below Cannot Be Reconciled with *Hughes* or This Court's Preemption Precedents

Respondents advance the same merits arguments that persuaded the lower court to go awry. The Petition details why these arguments are inconsistent with *Hughes* and this Court's approach to preemption, but Petitioners highlight a few flaws again here.

1. Respondents argue that the ZEC program is permissible because it regulates power *generation*,

citing *Northwest Central Pipeline*. NY Opp. 18–19, 27–28; Ex. Opp. 33–34. But *Hughes* forbids second-guessing or disregarding FERC-approved rates, *even when* the State is acting in an area traditionally reserved for state regulation. 136 S. Ct. at 1299. Indeed, before *Hughes*, the Court twice rejected State attempts to disregard federally approved wholesale rates where the challenged measures regulated a quintessential sphere of state authority: retail rates. See *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988); *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986). States have broad authority to regulate in-state generation, but cannot use that authority to "disregard[] an interstate wholesale rate required by FERC." *Hughes*, 136 S. Ct. at 1299.

2. Respondents invoke the purpose of the ZEC program and attempt to distinguish the Maryland subsidy this Court held preempted in *Hughes* on that basis. See, e.g., Ex. Opp. 30. *Hughes* prohibits this type of purposive inquiry. 136 S. Ct. at 1298 (States "may not seek to achieve ends, however legitimate, through regulatory means that intrude on FERC's authority over interstate wholesale rates"). But even on its own terms, Respondents' attempt to distinguish the Maryland program fails. Exelon claims that, unlike that program, "the ZEC Program does not, and does not need to, hijack FERC's wholesale markets to accomplish its aims" of "fight[ing] climate change and … reduc[ing] carbon emissions." Ex. Opp. 30. But the entire purpose of the ZEC subsidy is to ensure that nuclear generators that would otherwise be forced to retire stay in the wholesale marketplace even though they could not operate profitably at FERC-approved wholesale rates, purportedly

to advance New York's environmental goals. See Pet. 9–12. Thus, just as in *Hughes*, the State is disrupting the ordinary operation of the wholesale markets to accomplish its aims.

3. Exelon argues that Petitioners' reading of *Hughes* would have "sweeping effects" because "[m]any state programs provide payments to generators that sell exclusively at wholesale." Ex. Opp. 31–32. Exelon misunderstands Petitioners' argument. Petitioners do not contend that *Hughes* preempts *all* state efforts to promote the generation of electricity that will be sold at wholesale; rather, Petitioners argue that any subsidy that violates *Hughes*' prohibition against second-guessing or disregarding FERC-approved rates is preempted, regardless of whether receipt of that subsidy is expressly conditioned on wholesale market participation. The formalistic distinction drawn by the court below is inconsistent with *Hughes*. Pet. 23–27. Otherwise, Maryland could proceed with its preempted subsidy program "after a few tweaks to the wording." Monitor Br. 4.

Moreover, as the Petition demonstrates, such a constricted reading of *Hughes* is fundamentally incompatible with this Court's approach to preemption. Pet. 27–29. Tellingly, the New York State Respondents did not even argue that *Hughes* turns on the language of the program rather than how the subsidy operates, and Exelon's one-paragraph response is non-responsive. Ex. Opp. 32–33. The question is, as the Market Monitor aptly put it, "whether *Hughes* stands for a principle or is limited to semantics." Monitor Br. 4. The Court's preemption jurisprudence makes unequivocally clear that it must be the former.

4. Respondents persist in disputing the well-pleaded factual allegations of Petitioners' complaint. NY Opp. 25–27; Ex. Opp. 22–24. To the extent Respondents claim Petitioners did not allege certain facts, the complaint speaks for itself, Pet. App. 92a–129a; otherwise, Respondents' arguments are inapt in the Rule 12(b)(6) context,[3] see, e.g., *Fitzgerald v. Barnstable Sch. Comm.*, 555 U.S. 249 (2009) ("Because this case comes to us on a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), we assume the truth of the facts as alleged in petitioners' complaint.").

IV. The "Vehicle Problems" Identified by Respondents Are Non-Issues

Finally, Respondents claim "two threshold justiciability" questions not addressed by the decision below would hinder the Court's review: (1) whether there is a private cause of action for FPA preemption under *Armstrong v. Exceptional Child Center, Inc.*, 135 S. Ct. 1378 (2015), and (2) whether Petitioners have standing. Ex. Opp. 25–28; NY Opp. 23–25. Not so.

1. Because the existence of a cause of action is not a jurisdictional question, see, e.g., *Verizon Maryland, Inc. v. Pub. Serv. Comm'n of Maryland*, 535 U.S. 635, 642–43 (2002), the Court can reach the merits without deciding the *Armstrong* question—just as it did in *Hughes* and just as the Second Circuit did below. It would make little sense for the Court to leave undisturbed an incorrect interpretation of its

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[3] *Amici* corroborate the factual allegations Respondents dispute. E.g., Econ. Br. 6–7, 10–13.

own decision that is seriously impairing federal energy policy merely because there *might* be another ground for dismissal on remand.

2. Standing *is* a jurisdictional prerequisite, so the Second Circuit could not have reached the merits if there was any doubt about standing. Unsurprisingly, there was none. Petitioners allege that the ZEC subsidy "artificially depress[es]" FERC-mandated auction prices, resulting in "lower revenues" for non-favored generators, thereby causing Petitioners competitive injury. Pet. App. 95a, 122a, 124a (Compl. ¶¶ 6, 81, 87–88). These allegations establish injury-in-fact (loss of revenue) that is fairly traceable to the challenged State action (the ZEC program) and redressable by a favorable judgment (an injunction against enforcement of that program).

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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