Adopting State Feed-in Tariff Laws without Federal Preemption[1]

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As states move forward to adopt strong feed-in tariffs (FITs), concerns about federal preemption arise. This paper is intended to help renewable energy advocates understand the concerns about federal preemption[3] and understand possible paths forward for states to adopt robust FITs that are not preempted.[4] This paper does not attempt to describe what a FIT is or what a well-designed FIT should include, because other sources do that well.[5]

This paper is not intended as legal advice. Anyone working to promote a FIT law in their state should work with a local lawyer who will know best how to craft a law that works well with other existing laws in that state.

In October 2010, the Federal Energy Regulatory Commission (FERC) made it clear that states have the authority to adopt FITs to advance state goals of bringing more renewable energy into the grid.

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[1] This document is a work in process and comments, suggestions, and criticisms are welcome to ensure that renewable energy advocates have the best information available in their hands. Comments should be sent to jen [at] elaw.org. The latest version of this paper can be found on the website of the Environmental Law Alliance Worldwide at: http://www.elaw.org/node/5741 or the Alliance for Renewable Energy at http://www.allianceforrenewableenergy.org/.

[2] The paper is written by Jennifer Gleason, Staff Attorney for the Environmental Law Alliance Worldwide (ELAW) (http://www.elaw.org/). This paper was commissioned by the Alliance for Renewable Energy (ARE) (http://www.allianceforrenewableenergy.org/) with funds from the 11th Hour Project. ELAW and Jennifer Gleason are responsible for the content of the paper.

[3] The National Renewable Energy Laboratory (NREL) published Hempling et al., *Renewable Energy Prices in State-Level Feed-in Tariffs: Federal Law Constraints and Possible Solutions* (January 2010). This report offers a comprehensive review of the possible federal law constraints to states implementing well-designed renewable energy programs. Note that it was published before recent FERC decisions were issued which change part of the landscape.

[4] Note, however, that even if the law is well-written to avoid preemption, any law can be challenged.

[5] These issues are well-documented in other sources. *See*, for example, resources available on the websites of the Alliance for Renewable Energy (ARE) (http://www.allianceforrenewableenergy.org/) the World Future Council (http://www.futurepolicy.org/renewableenergy.html), Wind-Works (http://www.wind-works.org/articles/feed_laws.html), and the Clean Coalition (http://www.clean-coalition.org/).

THE FEDERAL POWER ACT

The Federal Power Act (FPA) grants the federal government jurisdiction over the "sale of electric energy at wholesale" which is further defined as a "sale of electric energy to any person for resale." FPA § 201. The Federal Energy Regulatory Commission (FERC) has sole jurisdiction over rates charged for electricity sold at wholesale.

There are at least four exceptions to this sole federal jurisdiction:

1. Alaska, Hawaii and Texas

The first exception is that the FPA does not regulate wholesale sales in Alaska, Hawaii and most of Texas because these electric grids do not cross state lines. Section 201 of the FPA only applies to sales in interstate commerce.[6]

2. Sales from State Agencies

The second exception is sales *from* the federal government, a state, or a subdivision of a state. The FPA states that it does not apply to sales from these entities (and a few others). FPA § 201(f).

3. PURPA

The third exception is that states have limited authority to set the rate for purchases of wholesale electricity under the Public Utility Regulatory Policies Act (PURPA). (FERC maintains jurisdiction to ensure that rates are just and reasonable).

PURPA requires electric utilities to purchase electricity generated by cogenerators and small power production facilities, which are known together as "qualified facilities" or "QFs."[7] The FPA defines a qualifying "small power production facility" as a facility that produces electric energy from biomass, waste, renewable sources or geothermal sources that has a power production capacity of not greater than 80 MW. FPA § 3(17)(A); 18 C.F.R. § 292.203. A qualifying cogeneration facility is defined in FERC regulations found at 18 C.F.R. § 292.205. The utilities are required to purchase electricity from QFs at what is known as *avoided costs*.[8]

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[6] The FPA states that "electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof . . . ." FPA § 201(c). Arguing that wholesale transactions in other states are not in interstate commerce will be difficult. See, *Federal Power Comm'n v. Florida Power & Light Co.*, 404 U.S. 453 (1972).

[7] The Energy Policy Act of 2005 added a provision to PURPA that allows FERC to relieve electric utilities from the mandatory purchase obligation if FERC determines that a QF has access to one of three types of markets outline in the law. PURPA § 210(m). FERC regulations state "there is a rebuttable presumption that a qualifying facility with a capacity at or below 20 megawatts does not have nondiscriminatory access to the market." 18 C.F.R. 292.309(d)(1).

[8] PURPA § 210 states that the rates that utilities must pay must be 'just and reasonable' and shall not exceed "the incremental cost to the electric utility of alternative electric energy." PURPA § 210(b). 'Incremental cost of alternative energy' is defined as "the cost to the electric utility of the electric energy which, but for the purchase from [a QF], such utility would generate or purchase from another source."

Avoided costs means "the incremental costs to an electric utility of electric energy or capacity or both which, but for the purchase from the qualifying facility or qualifying facilities, such utility would generate itself or purchase from another source." 18 C.F.R. § 292.101(b)(6). In plain English, avoided costs is the cost the utility would have incurred to generate its own electricity or to buy electricity from another source instead of buying electricity from a QF.

States are charged with determining "avoided costs" for purchases from QFs. Traditionally, avoided cost rates have been set as the cost of the least expensive power and capacity the utility could purchase without regard to the source of the electricity that was generated. That means that in a state in which the law prohibits utilities from adding a coal-fired power plant as a new generation source, natural gas is likely to be the least-expensive source of electricity that the utility could self-generate or go out and purchase from a third party, and avoided cost will be set at the cost of natural gas. Traditional avoided cost rates were too low to be used to implement a strong FIT.

However, a recent decision by FERC makes it clear that a state can make separate avoided cost calculations if the utility is required to procure electricity from different sources.[9] FERC's decision in *California Public Utilities Commission*, 133 FERC ¶ 61,059 (October 21, 2010), clarified by FERC in its order denying rehearing, *California Public Utilities Commission*, 134 FERC ¶ 61,044 (January 20, 2011) makes it clear that if a state requires utilities to purchase electricity from renewable sources, it may set avoided costs for the types of electricity that the utility must procure. Thus, if a state *requires utilities to purchase* 30 MW of electricity generated on solar photovoltaic (solar PV) systems with a total capacity of 10 kW or less, and 100 MW of electricity from solar PV systems between 10 kW and 100 kW, then the state should be able to set separate avoided costs for each of these categories and require utilities to purchase the electricity at that rate (until the utility has met each of these procurement requirements). If a state requires utilities to supply 30% of its electricity from renewable sources, then the state could set avoided cost at the rate needed to cover the least expensive eligible renewable source (this rate would apply only to sales needed to procure the 30%).

If a state is implementing a FIT following the formula described by FERC in the October, 2010 and January, 2011 orders, it would need to implement it under PURPA and sellers would need to be QFs.

OUTSIDE THE FEDERAL POWER ACT

There is also at least one way for a state to implement a FIT outside of these exceptions to the FPA without federal preemption. FERC has made it clear that renewable energy

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The regulations implementing PURPA state that "avoided costs" means the "incremental costs." 18 C.F.R. § 292.101(b)(6). Most people use the term "avoided costs."

[9] The recent FERC orders may have opened up other paths as well.

certificates (RECs)[10] have been created by the states and that the market for the RECs is controlled by the states. States have the authority to set the price for a REC. A FERC order states, "RECs are created by the States. They exist outside the confines of PURPA. . . . States, in creating RECs, have the power to determine who owns the REC in the initial instance, and how they may be sold or traded . . . ." *American Ref-Fuel Company*, 105 FERC 61,004 (October 1, 2003).[11] Therefore, a FIT could be designed so that a utility would have to purchase the electricity at avoided cost and purchase the accompanying REC at a price set by the state. Avoided cost could be traditional avoided cost rates if there is no renewable energy procurement requirement, or differentiated rates if there is a state procurement requirement in place. The seller would have to be a QF. Of course, this would only apply to a state that has created renewable energy credits or creates them as part of this process.

OTHER NOTES RELATED TO FEDERAL PREEMPTION

NET METERING

Net metering, a program that allows people to install renewable energy generating facilities and use the electricity on-site before sending any excess to the grid, and take electricity from the grid when they need more than they produce, can look like a wholesale transaction that would be preempted by federal law, but it is not. The Energy Policy Act of 2005 encouraged states to consider adopting net metering programs and many states have. Now some states are looking at enhanced net metering programs instead of instituting a true FIT. One reason for that is that FERC has said that as long as the generator does not generate more than it uses, the Commission will not assert jurisdiction over the program.[12] Net metering programs will not stimulate the market like a FIT.[13]

LONG TERM CONTRACTS

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[10] The Environmental Protection Agency (EPA) explains that "[a] REC (pronounced: rĕk) represents the property rights to the environmental, social, and other nonpower qualities of renewable electricity generation. A REC, and its associated attributes and benefits, can be sold separately from the underlying physical electricity associated with a renewable-based generation source. EPA Green Power Partnership, "What is a REC?" http://www.epa.gov/greenpower/gpmarket/rec.htm.

[11] The recent FERC orders mentioned above also note that compensation for the environmental attributes of electricity generated can be paid through purchase of a REC. See, for example: *California Public Utilities Commission*, 133 FERC ¶ 61,059 (October 21, 2010) at para. 31.

[12] "The Commission has explained that net metering is a method of measuring sales of electric energy. Where there is no net sale over the billing period, the Commission has not viewed its jurisdiction as being implicated; that is, the Commission does not assert jurisdiction when the end-use customer that is also the owner of the generator receives a credit against its retail power purchases from the selling utility. Only if the end-use customer participating in the net metering program produces more energy than it needs over the applicable billing period, and thus is considered to have made a net sale of energy to a utility over the applicable billing period, has the Commission asserted jurisdiction." Sun Edison, LLC., 129 FERC ¶ 61,146 (Nov. 19, 2009), para. 18 (footnotes omitted).

[13] See for example, Implementation Options and Recommendations for Net Metering and Feed-In Tariffs for Distributed Generation and Renewable Energy Sources within the European Union, May 2007, http://cleanenergysolutions.org/node/1370.

It should be noted that states have the authority to require utilities to enter into long-term contracts to purchase electricity from a particular source. In FERC's *California Public Utilities Commission* October 2010 Order, FERC made it clear that states have the authority to require utilities to purchase energy from particular sources "for a long duration."[14]

RENEWABLE ENERGY STANDARD OFFER

The American Council On Renewable Energy (ACORE) is working with the Federal Energy Regulatory Commission to define another path forward that would include FERC approving rates submitted to it by state public utility commissions.[15]

CONCLUSION

It is clear that states have the authority to adopt strong FITs. States can design a program that falls within one or more of the exceptions to exclusive federal authority under the FPA or they can design one that uses payments for RECs to supplement the price that will be paid for the electricity. To understand specifically how a state can implement a strong law, see the paper that accompanies this paper, *Available Paths for Designing Strong State Feed-in Tariffs.*

[14] *California Public Utilities Commission*, 133 FERC ¶ 61,059 (October 21, 2010), para. 26.
[15] If you would like more information, please contact (Ms) Jeramy Shays (shays [at] acore.org).