**Before**

**The Public Utilities Commission of Ohio**

In the Matter of the Application of Duke )

Energy Ohio, Inc., for the Establishment ) Case No. 12-2400-EL-UNC

of a Charge Pursuant to Revised Code )

Section 4909.18 )

In the Matter of the Application of Duke )

Energy Ohio, Inc., for Approval to ) Case No. 12-2401-EL-AAM

Change Accounting Methods )

In the Matter of the Application of Duke )

Energy Ohio, Inc., for the Approval of a ) Case No. 12-2402-EL-ATA

Tariff for a New Service )

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**Notice of Additional Authority**

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**Notice of Additional Authority**

In support of its demonstration that the Public Utilities Commission of Ohio (“Commission”) does not have jurisdiction to increase the amount of compensation provided to Duke Energy Ohio, Inc. (“Duke”) for the provision of wholesale generation-related capacity service (“Capacity Service”), Industrial Energy Users-Ohio (“IEU-Ohio”) provides Notice of Additional Authority. Attached is the decision of the United States District Court of Maryland in *PPL Energyplus, LLC, et al., v. Douglas R. M. Nazarian*, *et al*., Civ. Action No. MJG-12-1286 (decided Sept. 30, 2013) (“*PPL I*”), in which the District Court found that the Maryland Public Service Commission (“Maryland Commission”) was preempted from authorizing above-market compensation for the provision of wholesale energy and capacity service. Also attached is the decision of the District Court for the United States District Court of New Jersey in *PPL Energyplus, LLC, et al., v. Robert M. Hanna, et al.*, Civ. Action No. 11-745 (decided Oct. 11, 2013) (“*PPL II*”), in which the District Court found that the New Jersey Long-Term Capacity Pilot Project Act (“LCAPP”) was unconstitutional because it violated the Supremacy Clause.

In its Application and supporting testimony, Duke has repeatedly asserted that the Commission has jurisdiction to increase Duke’s total compensation for the provision of Capacity Service under Chapters 4905 and 4909, Revised Code, and the Reliability Assurance Agreement (“RAA”), an agreement among members of the PJM Interconnection, LLC (“PJM”), because the service is a wholesale service.[[1]](#footnote-1) In support, it argues that the compensation it receives under the federally-approved Reliability Pricing Model (“RPM-based Price”) is inadequate.[[2]](#footnote-2) Neither Ohio law nor the RAA, however, provides authority to approve an increase in compensation for Capacity Service established through the Reliability Pricing Model (“RPM”) Duke agreed to in its settlement of its last Electric Security Plan (“ESP”) case.[[3]](#footnote-3)

The recent decisions of the District Courts of Maryland and New Jersey provide an additional basis on which the Commission must dismiss Duke’s Application. The *PPL* decisions find that the Federal Power Act (“FPA”) preempts a state commission from approving an increase in total compensation of a generator for the provision of wholesale energy and capacity above the RPM-based Price.

***PPL I***

In *PPL I*, the plaintiffs challenged an order of the Maryland Commission directing the local electric distribution companies to compensate generators for the construction and operating costs of a new gas generation plant in an amount in addition to the wholesale compensation they received from PJM for capacity and energy.[[4]](#footnote-4)

Like Ohio, Maryland’s legislature enacted legislation in 1999 that restructured the retail electric generation industry and required that the generation business segment be separated from the distribution segment.[[5]](#footnote-5) Also like Ohio, the distribution company was responsible for supplying a default generation alternative, the Standard Offer Service, for those customers that did not contract with a competitive retail electric service provider.[[6]](#footnote-6)

In 2007, the Maryland legislature directed the Maryland Commission to study re-regulation options.[[7]](#footnote-7) In subsequent proceedings, the Maryland Commission questioned the ability of the wholesale market to relieve a potential capacity shortage, and it issued a request for proposals to secure additional capacity resources.[[8]](#footnote-8) Under the request for proposals, the generator would have to offer its capacity and energy to PJM and be compensated by PJM.[[9]](#footnote-9) In addition to the compensation for capacity and energy it received from PJM, the generator would also receive a payment from the local distribution companies under a long term contract that enabled the generator to receive a proposed contract price. As explained by the successful bidder in its response to the request for proposals, the costs it used to calculate the contract price included costs of construction of the generating plant, the fixed operating costs of going forward, such as labor, property taxes, and maintenance, financing costs of construction, and a reasonable rate of return.[[10]](#footnote-10) Electric distribution companies were ordered to enter into contracts to pay the generator the difference between what the generator received for energy and capacity from PJM and the contract-based total compensation.[[11]](#footnote-11) The electric distribution companies that paid the generator amounts in excess of the amounts the generator recovered from PJM for energy and capacity would then be authorized to recover the excess amount from their Standard Offer Service customers.[[12]](#footnote-12)

The District Court determined that the actions of the Maryland Commission approving the compensation structure which permitted the generator to recover revenue in excess of the RPM-based Price were preempted under the Supremacy Clause[[13]](#footnote-13) because the Maryland Commission’s pricing of wholesale capacity and energy sales invades a field occupied exclusively by the Federal Energy Regulatory Commission (“FERC”) under the FPA.[[14]](#footnote-14) While acknowledging that the Maryland Commission retained jurisdiction over matters such as siting, the Court went on to state that “after a generator physically comes into existence and operation and participates in the wholesale electric energy market, the prices or rates received by that generator in exchange for wholesale energy and capacity sales are within the sole purview of the federal government.”[[15]](#footnote-15) The Court continued:

While Maryland may retain traditional state authority to regulate the development, location, and type of power plants within its borders, the scope of Maryland’s power is necessarily limited by FERC’s exclusive authority to set wholesale energy and capacity prices under, *inter alia*, the Supremacy Clause and the field preemption doctrine. Based on this principle, Maryland cannot secure the development of a new power plant by regulating in such a manner as to intrude into the federal field of wholesale electric energy and capacity price-setting.[[16]](#footnote-16)

The intention of the Maryland Commission to fill a potential shortfall in capacity resources did not justify the Commission’s actions. “Where a state action falls within a field Congress intended the federal government alone to occupy, the good intentions and importance of the state’s objectives are immaterial to the field preemption analysis.”[[17]](#footnote-17) The critical fact was whether the state order set the total wholesale compensation received by the generator.[[18]](#footnote-18)

Based on the terms of the contract that allowed recovery of cost-based total compensation, the Court determined that the Maryland Commission’s order set a price for wholesale capacity and energy service.[[19]](#footnote-19) Having found that the Maryland Commission had set a price for wholesale capacity and energy service, the District Court concluded that the Commission’s actions were preempted: “[U]nder field preemption principles, the [Maryland Commission] is impotent to take regulatory action to establish the price for wholesale energy and capacity sales. FERC has exclusive domain in that field and has fixed the price for wholesale energy and capacity sales in the PJM Markets as the market-based rate produced by the auction processes approved by FERC and utilized by PJM.”[[20]](#footnote-20) Further, the Court stated:

Because states have no authority, either traditional or otherwise, to set wholesale rates, the compensation received by [the generator] for its wholesale energy and capacity sales is exclusively subject to regulation of FERC.  While there exist legitimate ways in which states may secure the development of generation facilities, *states may not do so by dictating the ultimate price received by the generation facility for its actual wholesale energy and capacity sales in the PJM Markets without running afoul of the Supremacy Clause*.[[21]](#footnote-21)

***PPL II***

In *PPL II*, the District Court’s decision finding LCAPP preempted and void again arose in a state in which state law mandates retail electric competition. Like Ohio and Maryland, the New Jersey legislature enacted legislation restructuring the retail electric generation business and its regulation in 1999.[[22]](#footnote-22) The legislation required New Jersey electric distribution companies to divest their generation assets and permitted retail customers to choose a generation supplier.[[23]](#footnote-23) Over the opposition of New Jersey officials, pricing of wholesale capacity resources in New Jersey was governed by PJM under RPM. Beginning in 2006, state leaders opposed the adoption of RPM based on concerns that RPM, transmission constraints, and the effects of environmental regulation would result in insufficient capacity to serve the state.[[24]](#footnote-24)

In response to the concerns regarding sufficient capacity resources, the New Jersey legislature enacted LCAPP in 2011.[[25]](#footnote-25) An express purpose of LCAPP and the contracts approved under the statute was to provide a transaction structure that would result in new power plant construction in the PJM region that would benefit New Jersey.[[26]](#footnote-26) To effect that purpose, the statute required New Jersey electric distribution companies to enter into long-term contracts with eligible generators selected through a competitive bidding process and pay the generators the difference between the RPM auction price and the “actual development costs” of the generator.[[27]](#footnote-27) (The approved contract for one generator required above-market payments to the generator for fifteen years).[[28]](#footnote-28)

Following analysis similar to that in *PPL I*, the District Court initially determined that LCAPP was preempted under field preemption because LCAPP supplants the FPA.[[29]](#footnote-29) To support that finding, the Court identified various terms of the LCAPP contracts that relied on RPM terminology and related specifically to the determination of a wholesale capacity price.[[30]](#footnote-30) The Court then determined that the field of wholesale electricity pricing was a field within the exclusive authority of FERC[[31]](#footnote-31) and that LCAPP and the New Jersey Board of Public Utilities (“NJ Board”) approved contracts sought to supplant the FPA by establishing the price that LCAPP generators would receive for their sales of wholesale capacity. Accordingly, LCAPP was preempted.[[32]](#footnote-32)

The District Court also held that there was a conflict between state and federal law that required the state law to be preempted. Under conflict preemption doctrine, a state law is preempted if it stands as an obstacle to the accomplishment of the purposes and objectives of Congress.[[33]](#footnote-33) If there is a conflict, the state law must yield regardless of the purpose the state seeks to pursue.[[34]](#footnote-34) The District Court held that LCAPP poses an obstacle to FERC’s implementation of RPM because the record demonstrated that LCAPP undermined competitors’ reliance on the price signals provided by RPM.[[35]](#footnote-35) “The effects … demonstrate that the [Commission-approved contract’s] imposition of a government imposed price creates an obstacle to [FERC’s] preferred method for the wholesale sale of electricity in interstate commerce.”[[36]](#footnote-36)

***The FPA Preempts Commission Wholesale Price Setting***

In this Application, Duke complains that it is not receiving sufficient revenue because it has agreed to accept only the RPM-based Price.[[37]](#footnote-37) It then seeks a formula-based increase in the total compensation it would receive for Capacity Service.[[38]](#footnote-38) Duke further states that the service for which it is seeking increased compensation is a wholesale service,[[39]](#footnote-39) relying on the Commission’s decision in the *AEP-Ohio Capacity Case*.[[40]](#footnote-40)

As demonstrated in the *PPL* decisions, the price setting of wholesale capacity and energy services is within the exclusive federal authority of FERC under the FPA. Based on well-understood principles that a state law or administrative action is preempted if it falls within a field Congress intended the federal government alone to occupy, the Commission is preempted from increasing the total compensation of Duke for wholesale Capacity Service.

The Commission’s motivation for increasing total compensation for Capacity Service does not provide a basis for avoiding the preemptive effect of the FPA. Policy justifications, whether based on the desire to increase available capacity resources as in Maryland and New Jersey or to protect the financial integrity of an electric distribution utility as the Commission has asserted in the *AEP-Ohio Capacity Case[[41]](#footnote-41)* and Duke urges in this case,[[42]](#footnote-42) do not provide any lawful justification. If the Commission order invades the field governed by the FPA, the order is preempted, regardless of the Commission’s purpose.

Likewise, an increase in the total compensation cannot be justified because all customers would be required to pay the increase through a nonbypassable “retail” charge. As shown by the decision in *PPL I,* authorization of a retail charge does not save the request for additional wholesale compensation from the preemptive effect of the FPA.

Accordingly, the FPA preempts the Commission from authorizing Duke’s requested increase in compensation for wholesale Capacity Service even if Ohio law provided the Commission a statutory basis to act (which it does not).

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Notice of Additional Authority* was served upon the following parties of record this 18th day of October, 2013, via hand-delivery, electronic transmission, or first class mail, U.S. postage prepaid.

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1. Application at 3; Duke Ex. 1 at 11. [↑](#footnote-ref-1)
2. *Id*. at 8. [↑](#footnote-ref-2)
3. Initial Brief of Industrial Energy Users-Ohio at 25-44 (June 28, 2013). [↑](#footnote-ref-3)
4. *PPL I* at 50-51 (copy attached). [↑](#footnote-ref-4)
5. *Id*. at 49-50. [↑](#footnote-ref-5)
6. *Id*. at 50-51. [↑](#footnote-ref-6)
7. *Id*. at 52. [↑](#footnote-ref-7)
8. *Id*. at 58. [↑](#footnote-ref-8)
9. *Id*. at 64. [↑](#footnote-ref-9)
10. *Id*. at 65. [↑](#footnote-ref-10)
11. *Id*. at 90-91. [↑](#footnote-ref-11)
12. *Id*. at 66. [↑](#footnote-ref-12)
13. U.S. Const., Art. VI, cl. 2. [↑](#footnote-ref-13)
14. 16 U.S.C. § 201 et seq. [↑](#footnote-ref-14)
15. *PPL I* at 85. [↑](#footnote-ref-15)
16. *Id*. at 85-86. [↑](#footnote-ref-16)
17. *Id*. at 86. [↑](#footnote-ref-17)
18. *Id*. at 87. [↑](#footnote-ref-18)
19. *Id*. at 88-93. [↑](#footnote-ref-19)
20. *Id*. at 93. [↑](#footnote-ref-20)
21. *Id* at 110-11 (emphasis added). [↑](#footnote-ref-21)
22. *PPL II* at 19. [↑](#footnote-ref-22)
23. *Id*. at 19-22. [↑](#footnote-ref-23)
24. *Id*. at 30-32. [↑](#footnote-ref-24)
25. *Id*. at 32. [↑](#footnote-ref-25)
26. *Id*. [↑](#footnote-ref-26)
27. *Id*. at 33. [↑](#footnote-ref-27)
28. *Id*. at 39. [↑](#footnote-ref-28)
29. *Id*. at 60. [↑](#footnote-ref-29)
30. *Id*. at 54-55. [↑](#footnote-ref-30)
31. *Id*. at 58-60. [↑](#footnote-ref-31)
32. *Id*. at 60. [↑](#footnote-ref-32)
33. *Id*. at 61. [↑](#footnote-ref-33)
34. *Id*. at 62. [↑](#footnote-ref-34)
35. *Id*. [↑](#footnote-ref-35)
36. *Id*. [↑](#footnote-ref-36)
37. Application at 4. [↑](#footnote-ref-37)
38. *Id*. at 4 & 7-8. [↑](#footnote-ref-38)
39. Id. at 3. [↑](#footnote-ref-39)
40. *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,* Case No. 10-2929-EL-UNC, Opinion and Order at 13 (July 2, 2012) (“*AEP-Ohio Capacity Case*”). [↑](#footnote-ref-40)
41. *Id*. at 23. [↑](#footnote-ref-41)
42. Application at 3. [↑](#footnote-ref-42)