

Regional Electricity Planning: Unavoidable Constraints, Possible Solutions

Scott Hempling, Esq.
Executive Director, National Regulatory Research Institute¹

- 1. Unavoidable Facts Relating to Regional Resource Planning**
- 2. Unavoidable Elements of an Effective Regional Resource Plan**
- 3. Unavoidable Legal Constraints Associated With Regional Resource Planning**
- 4. Possible Solutions: How Might We Integrate Regional Transmission Siting with Regional Generation Planning, While Satisfying All These Elements, Facts and Legal Constraints?**

* * *

I. Unavoidable Facts Relating to Regional Resource Planning

- A. For any generation or transmission project,
 1. some state must approve need and siting.
 2. some regulatory authority -- state or federal -- must approve the costs before they end up on a retail consumer's bill.
- B. For any given region, the least-cost combination of generation and transmission will involve sites, sellers and buyers in multiple states.
- C. A state that limits its options to projects located within that state -- raises costs for itself and other states.
- D. Without clear knowledge of the path to cost recovery, no one will invest in these projects.

¹ Presentation to the Western Conference of Public Service Commissioners, June 2009. The author's contact info is: 301-588-5385 ext. 304; shempling@nrri.org.

II. Unavoidable Elements of an Effective Regional Resource Plan

- A. If the plan is going to minimize total cost (taking into account constraints like environmental and siting laws), the plan must take advantage of resources available throughout a region.
- B. If the plan is going to ensure satisfaction of the public's needs (as opposed to private needs), then it must issue from, or be approved by, some government body.
- C. If the plan is going to produce a tangible result, then one or more government entities must have the power to order some private party to take action.
- D. For a plan to attract investment, the government must promise predictable cost recovery.
- E. For a plan to cover each state's needs, then each state must specify its needs and wishes concerning project types and project costs.
- F. If the plan involves wholesale transactions, it must receive approval from FERC.
- G. If the plan involves retail transactions, it must receive approval from each state commission regulating a retail utility that is bound by the plan.
- H. A utility should not have to prove prudence of the same project in multiple states.

III. Unavoidable Legal Constraints Associated With Regional Resource Planning

A. Constitutional Constraints

1. Compact Clause

"No State shall, without the Consent of Congress, ... enter into any Agreement or Compact with another State,..."

U.S. Constitution - Article 1 Section 10 Clause 3.

a. Implications: If states want to bind each other, contractually and enforceably, to --

(1) follow particular procedures in formulating a regional plan

- (2) allocate costs associated with a plan
 - (3) hire joint staff
 - (4) regulate utilities in a coordinated, consistent fashion,
- their agreement to do so requires Congressional approval.

b. The standard Compact process involves each state passing an identical law to join the Compact. Then Congress passes a law authorizing the Compact. A Compact need not be permanent. The federal authorizing legislation can include a sunset provision.

2. Takings Clause

"... [N]or shall private property be taken for public use, without just compensation."

U.S. Constitution, Fifth Amendment.

Implications: A government regulator must honor shareholders' legitimate, investment-backed expectations.

- (1) If regulators formally commit to a plan, and that plan promises utilities cost recovery if the utilities carry out that plan prudently, the regulators must order that cost recovery. They cannot change their mind about cost recovery unless they order a change to the plan before the utility incurs the costs.
- (2) The plan need not promise cost recovery. The plan can incorporate uncertainty about cost recovery. It can, for example, establish a cost cap or cost floor, in advance, and commit to determining actual cost recovery after costs are incurred. But to the extent it commits to cost recovery, the regulators must honor that commitment.

3. Commerce Clause

Congress has the power "[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;"

Article 1, Section 8, Clause 3

Implications: A state cannot discriminate in favor of its citizens and against citizens of other states.

- (1) The Supreme Court has interpreted the Commerce Clause as including two features: (a) a grant of power to Congress to regulate interstate commerce; and (b) a limit on the power of states to regulate interstate commerce. The second feature is sometimes called the "negative" or "dormant" Commerce Clause.
- (2) The dormant Commerce Clause ensures that buyers and sellers have access to a national market, free from undue interference by the states.
- (3) When acting as a regulator, a state may not protect its own economy from out of state competition, or discriminate against citizens of other states, or favor its own resources over the resources from other states.
- (4) A state may not block the construction of transmission or generation in its state on the grounds that the beneficiaries reside in some other state.
- (5) When acting as a regulator, a state may not insist that its utilities use in-state resources (such as coal produced by that state) to the exclusion of resources originating in other states.

4. Supremacy Clause

"This Constitution, and the Laws of the United States which shall be made in Pursuance thereof ... shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the contrary notwithstanding."

U.S. Constitution, art. VI, Paragraph 2.

- a. This provision, known as the "Supremacy Clause," means that federal law can nullify or preempt a state law. Whether a federal law preempts state law depends on congressional intent. Congress may signal its intent to preempt by passing laws directly, or by delegating its preemption authority to a federal agency.

- b. **Implications:** Because the transmission grid is interconnected across state lines, electricity flows in interstate commerce. Congress therefore has the constitutional power to preempt most aspects of state regulation of the electric industry. At present, Congress has preempted state law in the following areas:
- (1) sale of electricity at wholesale
 - (2) unbundled transmission of electricity
 - (3) reliability of the bulk power system (unless state actions are consistent with federal rules)
 - (4) siting of transmission (under special circumstances set forth in Section 216 of the Federal Power Act)
- c. Preemption examples: Transmission siting concepts under discussion in U.S. Senate (per Leon Lowery)
- (1) FERC preemption of all transmission siting, as in Natural Gas act
 - (2) FERC preemption of transmission siting for facilities exceeding a specified voltage
 - (3) FERC preemption of transmission siting for all "backbone" transmission facilities
 - (4) FERC preemption of transmission for transmission facilities that emerge from regional planning entities that make decisions after considering state and other views
 - (5) Expand the existing FERC preemptive authority (under Section 216 of the Federal Power Act) to all transmission facilities (instead of the present limit to facilities located in U.S. DOE-designated "National Interest Electricity Transmission Corridors")

B. State Law Constraints

1. Prejudgment

- a. In a matter that will culminate in an official order, a state commission (or commissioners) cannot commit itself to a result before considering, formally, all the record evidence.
- b. A state commission therefore cannot come to a meeting of regional state commissions, commit to a regional plan, and then return to its own state, hold a hearing, take evidence and then issue an order reflecting the commitment made before the hearing.

2. Ex parte

In a formal contested proceeding, a commissioner cannot discuss the substance with parties to that proceeding, except on the record.

3. Substantial evidence rule

A commission must base its decisions only on evidence that is in the record, not on evidence learned outside the record (unless the commission or a party places that evidence into the record).

IV. Possible Solutions: How Might We Integrate Regional Transmission Siting with Regional Generation Planning, While Satisfying All These Elements, Facts and Legal Constraints?

A. Premises

1. State commissions' traditional responsibility is to require, and ensure, that the local utility satisfies its retail load, reliably at reasonable cost, using the resource-types that the state prefers. If that state commission role is to continue, states must drive the regional process.
2. Each state desires access to the maximum feasible options. That desire requires access to the regional market.
3. The process breaks down if any state can take state-oriented transmission actions that block the generation desires of other states.

4. Access to the regional market therefore requires a regional transmission system, planned and operated to accommodate the needs specified by each state in the region.

B. An approach that does not require an interstate Compact

1. A regional entity would have legal responsibility for ensuring the existence and operation of transmission assets and access as necessary to create access to the collective generation needs desired by the region's states. That regional entity could be an "regional transmission organization" (RTO) or other type of entity.
2. The regional transmission entity would have the power to require construction of transmission, sited to minimize cost to the region, where that transmission is necessary to serve the collective generation needs of the region's states.
3. *Note:* This approach does not require a Compact, because the states are not making an agreement among themselves. Rather, the states are specifying their needs, arrived at independently. Those needs then drive the transmission decisions of the regional entity.

C. An approach that might require an interstate Compact

A regional plan, created through one of three paths, would have binding effect once approved by FERC. The plan would address the construction, cost allocation and cost recovery of generation, transmission and demand resource assets.

1. *State path:* Each state commission in a region approves, under state law, an identical plan. Upon submission to FERC of this plan, FERC approves it if it satisfies the traditional Federal Power Act tests: just and reasonable and not unduly discriminatory. For example, the plan could not impair the competitiveness of power supply or demand resource markets.
 - a. This approach would not require a Compact if each state somehow came to identical results without formally binding each other. That outcome is hard to imagine, given state laws against prejudgment and ex parte contacts and receipt of evidence off-the-record.
 - b. This approach would require a Compact if the state commissions wanted to meet formally and bind each other to a plan.
2. *Utility path:* One or more utilities could submit to FERC a regional plan. Again, FERC would approve the plan if it satisfies the traditional Federal

Power Act tests. Note: This utility path would be available only if the utilities first submitted the proposed plan to the affected states, and one or more state commissions (a) disapproved the plan, (b) failed to act within 12 months, or (c) lacked state statutory authority to approve the plan.

3. ***FERC path:*** FERC itself, or a non-utility intervenor, or one or more states, could initiate a proceeding at FERC to approve a plan. Again, FERC would approve the plan if it satisfies the traditional Federal Power Act tests. The affected states could require a pause in the FERC proceeding if (a) they notify FERC within 60 days of the FERC initiation of the proceeding that they wish to attempt the states path, and (b) approve, per the states path, their own plan within 12 months after issuing this notification.