

High Court Leaves NJ Power Plant Hopes Dimmed But Not Out

By Jeannie O'Sullivan

Law360, New York (April 21, 2016, 10:21 PM ET) -- A U.S. Supreme Court decision striking down subsidies for the construction of power plants in Maryland is likely the death knell for a similar program in New Jersey and sends officials back to the drawing board to look to drum up in-state energy production, although several alternatives could fill the void.

The justices on Tuesday backed the invalidation of Maryland's power plant subsidy program, agreeing with district and circuit courts that the incentives intended to spur in-state power plant construction there usurp the Federal Energy Regulatory Commission's authority over wholesale electricity markets. The New Jersey Board of Public Utilities had also sought the Supreme Court's review of a similar program that energy distributors successfully challenged in federal court.

But while the justices are scheduled to consider the BPU's petition on Friday, experts are betting the Garden State's program is facing the same fate as Maryland's and say that New Jersey's focus now should be finding a different way to encourage in-state energy generation that won't run afoul of the Supreme Court's recent guidance.

"New Jersey's program is certainly dead," said Donald M. Falk, a partner in Mayer Brown LLP's Palo Alto, California, office.

While the justices agreed with the Fourth Circuit that Maryland's program of sparking gas-fired power plant construction through long-term power purchase agreements with local utilities was preempted under the Federal Power Act, they did suggest that tax breaks, land grants or direct power plant subsidies were alternatives as long as they don't usurp "just and reasonable" wholesale rates set by FERC.

New Jersey, said Falk, has the same options as Maryland as long as it stays away from programs that are, as the justices said, "tethered to wholesale market transactions."

In challenging the programs, Talen Energy Marketing LLC, an Allentown, Pennsylvania-based electricity and natural gas distributor, and other companies had claimed the states' incentives artificially depress wholesale prices set by PJM Interconnection — a regional transmission organization serving 13 states, including New Jersey and Maryland, and regulated by FERC. The Fourth and Third Circuits agreed, respectively, in striking down the Maryland and New Jersey programs.

New Jersey had looked to the program, which Gov. Chris Christie signed into law in 2011, to help

diversify in-state energy production, as envisioned in an energy master plan that the state unveiled that same year.

Adding natural gas to the state's current mix of nuclear and renewable energy sources, according to the BPU, would help maintain lower wholesale prices for electricity and reduce emissions, among other benefits.

Known as the Long Term Capacity Agreement Pilot Program Act, the law established a system in which local electricity distributors would enter into a series of 15-year capacity agreements with companies aiming to build new power plants in the state.

Those agreements, known as standard offer capacity agreements, or SOCAs, would have set a long-term floor price for new electricity capacity, guaranteeing a steady revenue stream for plant developers and furthering the state's goal of adding 2,000 megawatts of generation per year. Officials had expected the program to generate a net economic benefit of \$1.8 billion over 15 years and create thousands of jobs.

"Energy is a vital tool of economic growth and job creation," BPU President Richard S. Mroz said in November, when the agency released an update of its energy master plan.

Three contracts were awarded under the program for plants that Hess-owned Newark Energy Center, NRG Energy Inc. and CPV Power Development would have developed. However, New Jersey and 12 other states must offer or "bid" power supply into the auction run by PJM. Only CPV Power and the Newark Energy Center projects cleared PJM's May 2012 capacity auction; NRG's project was canceled.

In defending the program in its high court petition, the BPU said the FPA charges FERC with regulating interstate electricity sales and transmission but leaves undisturbed the state's authority over plant construction, capacity and electricity purchasing decisions.

The Third Circuit's decision striking down New Jersey's program "contradicts the very premise upon which FERC initiated its regulation of future capacity auctions and disregards the FPA's allocation of authority between FERC and the states," the petition said.

New Jersey's case has garnered support from the New York State Public Service Commission, which also runs a competitive wholesale energy market, and contends New Jersey's subsidy payments don't set a rate but merely supplement auction prices. The rate, the NYSPSC said, remains the one set through FERC's capacity markets.

Asked about which alternatives, if any, it's considering to boost in-state energy production if New Jersey's program remains invalidated, a BPU spokesman said Thursday that the agency is reviewing the high court's decision in the Maryland case.

Michael Krancer, chair of Blank Rome LLP's energy industry team, insists that there are plenty of other options, as suggested in the high court's opinion.

States can procure additional capacity outside the PJM auction process through bilateral power purchase agreements, Krancer said, in which a buyer and seller exchange electricity for a fixed time. States could also construct their own generating plants and sell directly to their retail consumers, he said.

A third option would reverting to a “vertically integrated utility model” that would allow the state to retain full regulatory authority over its energy market, as opposed to ceding authority over wholesale interstate markets to FERC, Krancer said. But that alternative has a key drawback.

“The cost to that state’s consumers for power will skyrocket when any state would do that,” Krancer said. “Cutting power costs for consumers was the whole idea of going to competitive generation markets in the first place.”

But while New Jersey has options, the path ahead is still fraught with uncertainty.

The justices didn’t give outright approval of tax incentives, land grants, direct subsidies, construction of state-owned power plants or new regulations for the energy sector as alternatives, according to Day Pitney LLP partner David T. Doot. They merely said they “need not and do not address” their permissibility.

The court did make clear that state-ordered agreements in which there is no true transfer of power, just money, are unacceptable.

The high court disagreed with Maryland’s stance that its plan entails bilateral power purchase agreements — in which there’s a transfer of rights to buy and sell power, which is allowable — and instead found that the Maryland plan really just requires the transfer of money. That finding suggests that a true state-ordered bilateral power purchase agreement might pass muster, according to Doot.

That nuance was the fatal flaw of Maryland's program.

“We know if it’s like this, it’s in the unacceptable territory,” Doot said.

--Editing by Brian Baresch.
