ISSUE Alert | JULY 22, 2010

VanNess Feldman

FERC Issues First Major Ruling on Compatibility of State Feed-in Tariffs with Applicable Federal Energy Law

*By David Yaffe, Howard Shapiro, Van Smith**

In its first major ruling on state feed-in tariffs for renewable resources, the Federal Energy Regulatory Commission (FERC) partially rejected the State of California's proposal to require investor-owned utilities (IOUs) to purchase renewable energy from small renewable generators at state-prescribed prices. FERC has ruled that (1) the Federal Power Act (FPA) does not preempt the States from requiring IOUs to purchase wholesale electricity from combined heat and power generators (CHPs) that are not Qualifying Facilities (QFs) under Section 210 of the Public Utility Regulatory Policy Act (PURPA); (2) the FPA preempts the States from specifying the wholesale price for such purchases; (3) PURPA does not preempt the States from specifying the wholesale rates for purchases from CHPs that are QFs, provided such prices do not exceed the purchasing utilities' avoided cost rates; and (4) Federal jurisdiction under the FPA does not apply to state entities that are sellers under feed-in tariffs.[1]

These rulings were announced in a declaratory order proceeding initiated by the California Public Utilities Commission (CPUC) and California's three major IOUs. *California Public Utilities Commission*, 132 FERC ¶61,047 (Docket Nos. EL10-64-000 and EL10-66-000, issued July 15, 2010). A California statute, AB 1613, requires each IOU in California to file with the CPUC a standard-form ten-year power purchase contract, known as a "feed-in tariff." The mandated tariff is an offer by the IOU to buy, at a CPUC-set price, electricity generated by CHPs whose capacity does not exceed 20 MW. Like California, several European countries and Vermont now require load-serving utilities to purchase at specified rates the output of small-scale renewable and CHP generators, which are often located at end-user sites. The California Legislature had enacted the feed-in tariff requirement as part of comprehensive legislation aimed at reducing greenhouse gases. The CPUC's petition contended that the mandated feed-in tariffs were compatible with FERC's jurisdiction under Part II of the FPA and Section 210 of PURPA because the states alone have jurisdiction over their utilities' resource portfolios, and the FPA does not preempt California because it required only that such utilities make an *offer* to buy power. The IOUs' petition contended that the two federal statutes preempt AB 1613's feed-in tariff program.

THE DECLARATORY ORDER PROCEEDINGS

The CPUC filed a petition for declaratory order seeking approval of its implementing orders specifying the prices that the IOUs must offer for the output of CHP generators of 20 MW or less as an appropriate exercise

[1] Point (4) corrected from first edition.

* Van Smith is a Summer Associate at the firm.

of its authority to regulate purchaser utility procurement. The three affected California IOUs also filed a petition for declaratory order seeking invalidation of the CPUC's actions as preempted by FERC's exclusive authority to regulate the sale of electric power purchased for resale. FERC held that the California feed-in tariff structure was permissible only with respect to purchases of power from qualifying facilities under Section 210 of PURPA (cogeneration or small power production facilities) and only when the buy-back price does not exceed the utilities' avoided cost rates as permitted under Section 210 of PURPA.

More than 20 parties moved to intervene in the proceedings. Among the intervenors supporting the CPUC were the California Energy Commission, the California Attorney General, and various renewable and environmental groups. Intervenors opposing the CPUC included the Edison Electric Institute and the California Municipal Utilities Association (CMUA). CMUA also asked for other clarifications. The Sacramento Municipal Utility District (SMUD) took no position, but asked FERC to find that distribution level facilities and distribution-level feed-in tariffs for sales at distribution-level were beyond FERC's jurisdiction because they do not involve interstate bulk electricity sales and constitute local distribution expressly excluded from FERC's jurisdiction by FPA section 201(b).

THE FERC'S ORDER

FERC conceded that states may require non-QF utilities to purchase capacity and energy from specified resources. It held, however, that beyond such resource specification, the CPUC decisions constituted "impermissible wholesale rate-setting" preempted by the FPA because they set "rates for wholesale sales in interstate commerce by public utilities." It also held under existing precedent that the AB 1613 feed-in tariff program was *not* preempted to the extent it constitutes an implementation of PURPA, provided that (1) CHP generators eligible for contracts with the purchaser utilities obtain qualifying facility (QF) status under PURPA section 210 and the FERC's implementing regulations; and (2) the CPUC-set rates the purchaser utilities are required to offer do not exceed their avoided cost. Asserting, however, that no petitioner had requested it to determine whether the specific prices approved by the CPUC exceeded the California IOUs' avoided cost rates, FERC declined to address that question.

FERC explicitly rejected the arguments of the CPUC and many supporting intervenors that environmental considerations gave California jurisdiction, holding that such factors have no bearing on FERC's exclusive jurisdiction over wholesale rates. It also was unswayed by assertions that state estimates of environmental costs and benefits, *e.g.* reduction of carbon emissions, could be included in state avoided cost determinations for purchases from QFs. It reaffirmed that QF purchase rates may not exceed the purchasing utility's avoided cost as determined by the kinds of quantifiable information permitted under PURPA section 210 and the Commission's QF regulations.

FERC granted the CMUA's request for clarification that government-owned utilities exempted from its jurisdiction by FPA section 201(f) that are neither QFs nor public utilities are not affected by its decision. It rejected SMUD's assertion that it lacked jurisdiction over distribution-level facilities and feed-in tariffs. It

explained that the FPA grants it jurisdiction over all sales for resale in interstate commerce by public utilities without regard to the kind of facilities used to effectuate them.

SIGNIFICANCE

This decision is likely to be viewed as setting strict limits on the power of the States attempting to follow the lead of California and Vermont by prescribing wholesale prices for environmentally favorable forms of electric energy. States may, however, continue to mandate that IOUs purchase power and energy from environmentally-friendly sources, so long as such mandates do not set wholesale rates. The clarification granted to CMUA may provide some flexibility for those governmental, municipal and cooperative utilities exempted from FERC's FPA jurisdiction under Section 201(f).

FOR MORE INFORMATION

Van Ness Feldman regularly represents energy clients in FERC and state-level regulatory proceedings, including qualifying facility and exempt wholesale generator proceedings, and provides counsel on cost-based and market-based generation tariff development. If you are interested in additional information regarding FERC's ruling, please contact David Yaffe at (202) 298-1840, Howard Shapiro at (202) 298-1884, or Jay Ryan at (202) 298-1878.

© 2010 Van Ness Feldman, P.C. All Rights Reserved.
This document has been prepared by Van Ness Feldman for informational purposes only and is not a legal opinion, does not provide legal advice for any purpose, and neither creates nor constitutes evidence of an attorney-client relationship.