ORAL ARGUMENT NOT YET SCHEDULED

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

NEXTERA ENERGY RESOURCES, LLC, *et al.*, Petitioners,
v.
FEDERAL ENERGY REGULATORY COMMISSION, Respondent.
Case No. 17-1110

On Petition for Review of Orders of the
Federal Energy Regulatory Commission

REPLY BRIEF OF PETITIONERS NEXTERA ENERGY RESOURCES, LLC, THE NRG COMPANIES, AND THE PSEG COMPANIES

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GLOSSARY

Commission	Federal Energy Regulatory Commission, the Respondent
FERC	Federal Energy Regulatory Commission, the Respondent
FPA	Federal Power Act
ICAP	Installed Capacity
ICR	Installed Capacity Requirement
ISO-NE	ISO New England Inc.
LOLE	Loss of Load Expectation
MW	Megawatt
Net ICR or NICR	Net Installed Capacity Requirement
NYISO	New York Independent System Operator, Inc.
Order	*ISO New England Inc.*, 147 FERC ¶61,173 (2014), JA____-__.
PJM	PJM Interconnection, L.L.C.
Rehearing Order	*ISO New England Inc.*, 150 FERC ¶61,065 (2015), JA____-__.
Remand Order	*ISO New England Inc.*, 155 FERC ¶61,023 (2016), JA____-__.
Remand Rehearing Order	*ISO New England Inc.*, 158 FERC ¶61,138 (2017), JA____-__.

SUMMARY OF THE ARGUMENT

This case is not about whether states can or should promote the construction of new wind and solar generation resources to achieve environmental objectives, or what those objectives should be; it is about who *pays* for the state-mandated transformation of the energy sector in New England. Neither the Federal Power Act ("FPA") nor the ISO New England Inc. ("ISO-NE") market rules prevent states from promoting renewable generation through state-mandated contracts. Nothing prevents those resources from selling the energy they produce, which is how the overwhelming majority of generation revenues are earned. The question presented here is whether those resources will *also* receive a capacity payment, despite the fact that they are too expensive to clear the capacity market if they offer at their true cost. Here, the only function of the renewable entry exemption FERC authorized below is to shift the costs of state-mandated wind and solar generation contracts from the states' constituent-consumers to competitive merchant generators (including competitive renewable resources) by artificially lowering the price of generation capacity to mask the true cost of state-mandated uneconomic entry. Petitioners contend this scheme is unjust, unreasonable, and unduly discriminatory. And that was the law according to FERC, until now.

FERC's orders below reverse FERC's interpretation of its statutory mandate under the FPA and radically change the purpose of the ISO-NE Forward Capacity

Market. Before this case, FERC and the federal courts repeatedly affirmed the principle that the FPA both authorizes and requires FERC to prevent state-sponsored generation resources from artificially suppressing wholesale capacity prices. The clear rule was that states must bear the risk of "paying twice" to promote preferred resources that are too expensive to clear a capacity auction. Here, FERC reinterpreted the FPA, and also retroactively redefined the purpose of the Forward Capacity Market, to require that consumers should not be forced to buy "redundant" capacity. But that is precisely the same "paying twice" rationale FERC and the courts previously rejected. The only reason "redundant" capacity will exist is because states require their utilities to contract with uneconomic resources that cannot clear the capacity auction. Indeed, the only reason FERC gave for reversing itself is that states decided "those resources will be constructed with or without a renewables exemption." If that is so, it is irrational and inequitable for FERC to transfer the costs states deliberately choose to impose on their constituent-consumers by shifting those costs to competitive generators.

FERC argues that the artificial price suppression the exemption causes is acceptable because the damage is "limited" and FERC "balanced" the competing interests of competitive generators and consumers. Those claims are nothing more than pretty words here, where FERC's entire position rests on one paragraph of ISO-NE's testimony offering loose conclusions devoid of supporting data.

FERC's orders do not reflect a reasoned "balance" of competing interests. First, FERC cannot claim to balance the interests of generators and consumers when it makes no effort to determine, even roughly, what the price impact of the exemption will be. Without knowing that, FERC has no fulcrum to balance anything. Worse, FERC wrongly claims it has no duty to assess the financial impact of its decisions, notwithstanding contrary instructions from the Supreme Court and this Court explaining FERC's duty of reasoned decisionmaking under the FPA and Administrative Procedure Act ("APA"). Second, FERC cannot claim to balance competing interests when it fails to acknowledge that price suppression will occur at all. On brief, as in its orders below, FERC perpetuates the nonsensical fiction that price suppression is only a "potential" outcome. It is a mathematical fact the exemption can only lower prices. And third, FERC cannot claim to balance competing interests when it denies that generators are "paying for" anything at all, while simultaneously stating the express purpose of the exemption is to reduce capacity prices. This is just agency double-speak.

FERC's claim that the exemption is "narrow" or "limited" is also spurious. Here, those words mean anything less than a categorical exemption.

First, FERC cannot claim the exemption is limited when it is perpetual. It proceeds relentlessly to chew away at unsubsidized generation by displacing up to 200 MW of the competitive market per year. Nor can FERC claim the exemption

is limited when it offers no explanation at all for the 600 MW perpetual rollover for any unused portion of annual limit. Those limits only affect the speed at which state-mandated resources displace competitive resources, not the ultimate quantity.

Second, FERC cannot claim the exemption is meaningfully limited by a sloped demand curve when it does not determine, even roughly, how that curve will affect prices and then modifies the demand curve in a separate proceeding to cause even lower prices while this case is still pending. The unrebutted record evidence in this case shows the exemption would permit significant price suppression even before FERC's recent demand curve modifications. And FERC cannot sweep this aside as a dispute between conflicting experts. ISO-NE's witness failed to provide any economic data to support his conclusions about the exemption because, as ISO-NE conceded, its economic analysis of the sloped demand curve was prepared before the exemption was proposed. And FERC wrongly claims ISO-NE assumed a flatter supply curve than Petitioners did: Dr. Hunger used ISO-NE's supply curve and Mr. Schnitzer used an even flatter one.

Third, FERC's cannot claim anticipated load growth will limit the price suppression caused by the 200 MW annual exemption when the exemption is not actually tied to load growth and load has constantly declined. Worse, FERC knew wholesale load had declined and would continue to decline when it took this case

back on remand. No precedent holds that a federal agency may base its decision on information it knows is false when the decision is made.

Fourth, FERC cannot reasonably replace its original emphasis on load growth as a limiting factor with a new reliance on anticipated retirements. FERC's retirement claim was barely uttered in its initial orders and, as with ISO-NE's load estimates, the retirement estimates were greatly inaccurate.

Finally, FERC attempts to evade the manifest problems with its analysis of the exemption beforehand by stating that only 102 MW of subsidized resources have entered the market through the renewable exemption in the three capacity auctions held while this case was pending. That may be less than the exemption allows, but it has already shifted $324.6 million in capacity payments from competitive generators to more expensive renewable resources. FERC overlook the time it takes for states to formulate new contracts. Emboldened by FERC's exemption, New England states procured more than 800 MW of new renewable resources in 2017. FERC's carry-forward exemption allowance will permit more than 500 MW of those new projects to take capacity payments by offering themselves at no cost into the February 2018 capacity auction.

And now, three days before this brief, ISO-NE has filed fundamentally new capacity market rules to create Competitive Auctions with Sponsored Policy Resources, or "CASPR," because the current renewable exemption is insufficient

to permit the entry of new "clean energy procurements in the range of 2,800 MW" required by state law. *ISO New England Inc.*, Docket No. ER18-619, Transmittal Letter at 3-4 (Jan. 8, 2018).

For these reasons, this Court should vacate and remand FERC's orders to require a more reasoned basis for the systematic elimination of competitive generation in New England.

ARGUMENT

I. THE WISDOM AND LAWFULNESS OF STATE POLICIES PROMOTING A TRANSITION TO RENEWABLE RESOURCES ARE NOT AT ISSUE

A recurring theme in the opposing briefs is the suggestion that the renewable exemption was necessary to enable New England states to achieve laudable environmental objectives. *See* FERC Br. 17, 18, 20, 35-36, 40-41, 45, 48-49, 51; Int. Br. 4-6, 25-27; Amicus Br. 4, 5-9. That theme is misleading. The only question presented here is who should pay to achieve those state-mandated objectives; specifically, whether state-mandated resources should collect revenues from the capacity market, in addition to energy revenues and subsidies, when those resources are too expensive to clear the capacity market if they offer at their true cost. Petitioners reiterate that this case is *not* about the merits of renewable resources as compared to any other form of generation; it is about the unjust, unreasonable, and unduly discriminatory effects of deliberately authorizing uneconomic entry, regardless of generation type. Pet'r Br. 27 & n.5.

The New England States have chosen to pursue ambitious environmental goals by subsidizing renewable resources and by exercising their jurisdiction over retail rates to require their constituent-consumers to buy the energy those renewable resources generate. *See, e.g.*, FERC Br. 20, 54-55; Int. Br. 4-6, 20, 27, 32; Amicus Br. 5-9, 25-26. The FPA does not bar states from doing either of those things if the subsidies are untethered from the wholesale market. *See Hughes v. Talen Energy Mktg., LLC*, 136 S. Ct. 1288, 1299 (2016); *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 481 (D.C. Cir. 2009) ("*CTDPUC*"). And the ISO-NE minimum offer price rules did not prevent states from those things either, even before FERC accepted the exemption at issue here.

The ISO-NE market rules expressly permit generators to interconnect and participate in the wholesale market as energy-only resources, regardless of whether those resources also earn a capacity payment by clearing an annual or incremental capacity auction. *See* ISO-NE Tariff § II.47.1; *id.* Schedule 22, § 3.2. Indeed, there are many such energy-only resources currently operating in ISO-NE.[1] This is possible because the overwhelming majority of generator revenues are derived

[1] There are over 800 individual energy-only generating resources interconnected to the ISO-NE system with a combined capacity of over 1,000 MW. The formal name for these energy-only resources is Network Resource Capability ("NRC"), as distinguished from capacity *and* energy resources classified as Capacity Network Resource Capability ("CNRC"). *See* ISO-NE, CELT Report: 2017-2026 Forecast Report of Capacity, Energy, Loads, and Transmission, Tab 5.1 (May 1, 2017), Resource NRCs and CNRCs, https://www.iso-ne.com/static-assets/documents/2017/05/2017_celt_report.xls.

from selling energy and ancillary services, not capacity. The capacity market allows competitive generators to recoup their long-run marginal costs, because competition in the energy market drives prices down to short-run marginal costs, creating a "missing money" problem that would compromise system reliability by forcing the closure of generators whose energy sales are limited to serving peak demand or temporary outages. When a generator is not required to compete to sell energy—because, for example, a state requires its retail utilities to purchase energy from that generator—that generator has no "missing money" problem to correct.

In short, the renewable resource exemption FERC approved below was not necessary to permit new renewable resources to enter the wholesale market. *Contra*, *e.g.*, Amicus Br. 4, 5, 9-13. Nothing prevents New England states from constructing those resources or prevents those resources from selling energy and ancillary services in the New England wholesale market. The exemption simply provides a bonus revenue stream from the capacity market—in addition to energy sales and state subsidies—even though the resources that enter through the exemption are, by definition, too expensive to clear that market. The only way to secure those payments is to pretend the new resources cost less than they actually do by artificially lowering the capacity clearing price of every other resource in the market (including, ironically, other renewable resources). The exemption merely

shifts the costs of state-mandated resources from the states' constituent-consumers to competitive generators, regardless of generation type.

This allows the political entities that compose the New England States Committee to escape transparent accountability for the policies they have chosen to pursue. And it allows advocacy groups like the amici to achieve a double-windfall by financially advantaging new renewable resources while injuring nuclear and fossil-fired resources at the same time. But it is no part of FERC's statutory charter to "accommodate" either of those objectives. *Contra* FERC Br. 40-41 (citing Remand Order P 23, JA ___; Remand Rehearing Order P 68, JA ___). As the new FERC Chairman assured the Senate during his nomination hearing, "FERC is not an entity whose role includes choosing fuels for the generation of electricity." Senate Comm. on Energy and Nat. Res., Nomination Hearing (Sept. 7, 2017), https://www.energy.senate.gov/public/index.cfm/hearings-and-business-meetings?ID=1F2B5ABA-A677-48D1-8218-44C348A26B5D.

It is irrelevant that the New England states are interested in pursuing environmental objectives. *See, e.g., N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74 (3d Cir. 2014) ("*NJBPU*"); *CTDPUC*, 569 F.3d at 481. Those external objectives are no more significant to FERC's economic regulation mission than preserving jobs or fuel diversity by retaining coal and nuclear plants. Yet, while this case was pending, FERC prevented attempts to subsidize coal and nuclear resources through

state-mandated contracts in Ohio. *See Elec. Power Supply Ass'n v. FirstEnergy Solutions Corp.*, 155 FERC ¶61,101 (2016). Preemption cases against nuclear subsidies enacted by New York and Illinois are now pending in the Second and Seventh Circuits. *See Coalition for Competitive Elec. v. Zibelman*, No. 17-2654 (2d Cir. filed Aug. 25, 2017); *Village of Old Mill Creek v. Star*, Nos. 17-2433 *et al.* (7th Cir. filed July 17, 2017). And, days before this brief was filed, FERC rejected a Department of Energy rulemaking proposal that would have required special payments to prevent nuclear and coal plants from retiring. *See Grid Reliability and Resilience Pricing*, 162 FERC ¶61,012 (2018).

II. AUTHORIZING SYSTEMATIC PRICE SUPPRESSION TO ACCOMMODATE STATE POLICIES CONTRADICTS GOVERNING PRECEDENT DESCRIBING FERC'S STATUTORY MANDATE

A. FERC Erroneously Claims It Did Not Depart From Precedent

It is beyond serious dispute that FERC's orders below depart from FERC precedent defining its statutory duty to prevent artificial price suppression through uneconomic entry, that those orders were affirmed by this Court and the Third Circuit, and that the Supreme Court has relied upon those FERC orders and judicial opinions to hold that certain state-mandated capacity contracts are preempted by federal law. *See* Pet'r Br. 26-31 (collecting cases). FERC's orders on remand concede that its position "has evolved." Remand Order P 68, JA____; Remand Rehearing Order P 58, JA____-__; *see id.* P 48, JA____. Nevertheless,

the final section of FERC's brief contends that "The Commission Did Not Depart from Precedent," FERC Br. 46, before ironically concluding with two paragraphs that attempt to justify why FERC reversed itself, *see id.* at 54-56.

FERC's position—echoed by the intervening New England States Committee on Electricity—is that nothing in the prior decisions of FERC or reviewing courts constrained FERC from changing its position by accepting a more "limited" level of artificial price suppression than those FERC had previously rejected. *See* FERC Br. 46-56; Int. Br. 29-33. In FERC's view, "There Is No Bright Line Rule Concerning Price Suppression," because the only thing FERC is required to do is "balance" various competing interests before rendering a decision. FERC Br. 51-56; *see* Int. Br. 23, 31. FERC creatively turns judicial precedent upside down by pointing to language finding that FERC did not act arbitrarily and capriciously when it enacted minimum offer price rules to prevent artificial suppression of wholesale capacity prices through state-mandated procurement—that is, when FERC reached precisely the opposite conclusions that FERC reached in its decisions below. *See* FERC Br. 35-36 (citing *New England Power Generators Ass'n v. FERC*, 757 F.3d 283, 286 (D.C. Cir. 2014) ("*NEPGA*"), and *NJBPU*, 744 F.3d at 109); *id.* at 42-43; Int. Br. 31-32. It is difficult to see how FERC could ever "depart from precedent" if FERC orders and judicial decisions

affirming diametrically opposed results do not suffice. FERC's contrary argument is little more than a restatement of the standard of review. *See* FERC. Br. 43.

Prior to this case, there was indeed a "bright line rule concerning price suppression." *Contra* FERC Br. 51. FERC used very strong language to describe its statutory role because states were equally aggressive in arguing FERC had exceeded its authority by first creating capacity markets and then creating minimum offer price rules to prevent those markets from being gamed. FERC's unambiguous position was that "all uneconomic entry has the effect of depressing prices below the competitive level." *N.Y. Indep. Sys. Operator, Inc.*, 124 FERC ¶61,301 at P 29 (2009); *see PJM Interconnection, L.L.C.*, 128 FERC ¶61,157 at PP 87, 90 (2009). In *NEPGA*, this Court noted "FERC specifically found that '[out-of-market] capacity suppresses prices regardless of intent.'" 757 F.3d at 292 (quoting *ISO New England Inc.*, 135 FERC ¶61,029 at P 170 (2011)). And this Court explained why permitting states to insert uneconomic resources into the capacity market constitutes "definitional market distortion in favor of buyers." *NEPGA*, 757 F.3d at 294.

The Third Circuit likewise found the intent of "state and local policies and objectives with regard to the development of new capacity resources" was irrelevant when it specifically affirmed FERC's assertion that it is "forced to act . . . when subsidized entry supported by one state's or locality's policies has the

effect of disrupting the competitive price signals." *NJBPU*, 744 F.3d at 100-01 (quoting *PJM Interconnection, L.L.C.*, 137 FERC ¶61,145 at P 3 (2011)), *quoted in Hughes*, 136 S. Ct. at 1296. Adopting this Court's position when it affirmed the creation of the ISO-NE Forward Capacity Market, the Third Circuit held that states in PJM remain "free to make their own decisions" regarding the type and quantity of generation resources they prefer, "but they 'will appropriately bear the costs of [those] decision[s],' including possibly having to pay twice for capacity." *NJBPU*, 744 F.3d at 97 (quoting *CTDPUC*, 569 F.3d at 481). As FERC held the first time the states sought a narrower version of the exemption at issue here, "if the states choose to build uneconomic resources outside of the [Forward Capacity Market] pursuant to current or future initiatives to further various policy interests, the states, not the [Forward Capacity Market] are responsible for procuring redundant capacity." *New England States Comm. on Elec. v. ISO New England Inc.*, 142 FERC ¶61,108 at P 34 (2013) ("*NESCOE*").

That is a clear rule and it is silly for FERC to pretend it did not "depart from precedent" when it held below that "[t]he renewables exemption fulfills the Commission's statutory mandate by protecting consumers from paying for redundant capacity." Remand Order P 33, JA____.

FERC places far too much weight on the absence of a minimum offer price rule for renewable resources in PJM. *See* FERC Br. 49-50. As FERC previously

held, any exemption proposal in ISO-NE "must do more than rely on findings specific to PJM." *NESCOE*, 142 FERC ¶61,108 at P 37. In the PJM litigation, FERC was confronted with a rate modification under FPA section 205 and a complaint under FPA section 206 that were both directed at an immediate threat: decisions by New Jersey and Maryland to require contracts with state-selected natural gas resources. Neither filing sought to apply the minimum offer price rule to nuclear, coal, or renewable resources because the states in PJM—home of the giant Marcellus and Utica shale gas fields opened by fracking—were not aggressively subsidizing those types of generators. Here, the states are aggressively pursuing renewable subsidies and the purpose of the exemption is to systematically lower capacity prices. *See, e.g.*, Remand Order P 33, JA____.

B. The Renewable Exemption Undermines the Purpose of the Forward Capacity Market

This Court should not permit FERC to redefine the purpose of the FCM to suit its needs in any given situation. Unlike FERC's re-interpretation of its statutory mandate, which FERC eventually conceded "has evolved," *e.g.*, Remand Order P 68, JA____, FERC does not acknowledge that it has radically redefined the purpose the Forward Capacity Market in this case, pretending that nothing has changed. This Court has previously remanded FERC orders that attempted to sidestep arguments FERC was undermining the purpose the Forward Capacity

Market. *See PSEG Energy Res. & Trade LLC v. FERC*, 665 F.3d 203, 210 (D.C. Cir. 2011). It should do so again here.

Petitioners have repeatedly reminded FERC that the "purpose of the [Forward Capacity Market] is to attract and retain sufficient capacity to maintain ISO-NE's Installed Capacity Requirement, and to do so, [Forward Capacity Market] *capacity prices will need to average out over time to the cost of new entry*." *ISO New England Inc.*, 125 FERC ¶61,102 at P 43 (2008) (emphasis added). FERC's initial orders ignored Petitioners' argument that the renewable exemption directly contradicts that purpose by systematically and artificially reducing capacity prices below the price set by competition in capacity auctions. *See* Pet'r Br. 34-35 (summarizing record pleadings and testimony). Confronted with this argument again on remand, *see* Remand Rehearing 24-34, JA____-__, FERC chose to pretend there was no conflict by redefining the purpose of the market as follows: "It is the purpose of the [Forward Capacity Market] to attract and retain sufficient capacity to meet ISO-NE's *reliability targets* on average over time, *at least cost to customers, given the renewable generation that will enter as a result of state programs*." Remand Rehearing Order P 58, JA____ (emphasis added). Worse, FERC wrongly suggested Petitioners agreed with FERC's revisionist formulation. *See id.* P 24, JA____, *quoted in* Int. Br. 3.

There is no way to reconcile FERC's conflicting statements about the purpose of the Forward Capacity Market. The only thing those statements have in common is that ISO-NE must procure a sufficient quantity of capacity to operate the transmission system reliably, which ISO-NE is obliged to do regardless of whether a market exists. The purpose of the capacity market is to set an economically efficient price for that capacity, but FERC's reformulation in its orders on remand completely changes what that means. FERC simply abandons two bedrock principles: first, that competition is the best way to discover what a just and reasonable rate is; and second, that a just and reasonable rate will closely approximate the cost of new entry.

As Petitioners have explained, *see, e.g.*, Pet'r Br. 41, capacity prices can never "average out over time to the cost of new entry" when the exemption always lowers prices below the cost of new entry determined by competition to make way for explicitly uneconomic "renewable generation that will enter as a result of state programs." Remand Rehearing Order P 58, JA____. That definitely ensures "least cost to customers," *id.*, but only by distorting prices to shift the higher cost of that uneconomic new generation to competitive generators. *See* Pet'r Br. at 34-36 (summarizing record pleadings and testimony).

On brief, FERC continues to pretend that its orders did not redefine the purpose of the Forward Capacity Market. On the contrary, FERC claims it would

be "inconsistent with the purpose of the capacity market," as reformulated in the remand orders, *not* to create an exemption for state-sponsored resources. FERC Br. 38. FERC points to its statement below that, "[i]f renewable resources are being built, but are not reflected in the [market], then the [market] may send an incorrect signal to construct new capacity that is not needed." *Id.* at 38-39 (quoting Remand Rehearing Order P 9, JA ___). FERC says this is unacceptable because ISO-NE claimed it would be "economically inefficient." *Id.* at 39 (quoting Ethier Test. 39, JA____). FERC then says that such "efficiency concerns" are "in keeping with precedent and entirely appropriate." FERC Br. 39.

Yes, all parties and the Court can agree that FERC should "'promote the efficient use of, and investment in, generation, transmission, and consumption' of wholesale electric power in specific energy capacity systems.'" *Id.* (quoting *NEPGA*, 757 F.3d at 286 (citation omitted). But FERC's claim to promote economic "efficiency" in this case is spurious because FERC has abandoned the single economic efficiency metric on which the entire capacity market has been organized: whether prices average over time to the cost of new entry. Here, FERC *knows* it is creating a false price signal by specifically authorizing renewable resources to enter the capacity market at prices well below their actual cost, and to collect a capacity payment for doing so, thus allowing states to recoup the cost of subsidized renewable resources through lower market-wide clearing prices.

The revised price is deliberately inaccurate and there is nothing "efficient" about it. FERC's contention that this price distortion is necessary to prevent the potential construction of "redundant" capacity is Orwellian. As FERC correctly explained in *NESCOE*, 142 FERC ¶61,108 at P 34, the decision to create "redundant" capacity is not made by competitive generators; it is made by state regulators who decide to mandate new renewable resources regardless of whether they are too expensive to clear the market. The chief beneficiaries of the exemption are state regulators, who escape accountability for the consequences of their decisions to impose above-market contracts on their constituent-consumers. *See, e.g.*, Remand Rehearing 29-30 & nn.86-87, JA____-__. But the FPA does not authorize or require FERC to permit uneconomic entry when states decide for their own reasons "to limit new construction to more expensive, environmentally-friendly units." *CTDPUC*, 569 F.3d at 481.

C. FERC's Sole Justification for Reversing Its Statutory Principles and Revising the Purpose of the Forward Capacity Market Is Irrational and Inequitable

The essential question on judicial review is not whether FERC has "departed from precedent"—which, of course, it has—but whether FERC has provided "good reasons for the new policy." *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515-16 (2009). At the conclusion of its brief, FERC acknowledges the only justification it provided below for reversing its policy was that "states have

'continue[d] to support the development of renewable resources, which customers pay for through out-of-market mechanisms.'" FERC Br. 54-55 (quoting Remand Rehearing Order P 43, JA____). More bluntly, its "acceptance of the renewables exemption is an acknowledgement that those resources will be constructed with or without a renewables exemption." Remand Order P 62, JA____-__; *accord* Remand Rehearing Order P 48, JA____-__. That explanation is neither rational nor equitable. *See* Pet'r Br. 30-31.

First, it is difficult to imagine a more bankrupt reason than acquiescence to justify reversing a federal agency's conception of its statutory duty. Acquiescence to injurious conduct does not justify that conduct, but only encourages it. Test the validity of FERC's rationale against other prohibited behavior—for example, *malum in se* acts like theft or murder—and it clearly fails. It fails against *mala prohibita* conduct as well. Even the most ardent libertarian champion of limited regulation would hesitate to make someone else (here, competitive generators) pay for another person's choices (here, state-mandated contracts for preferred renewable resources). If those comparisons seem unfair, then test FERC's rationale against the minimum offer price rule in PJM if Maryland and New Jersey decided to call the federal government's bluff and enforce their state-mandated gas-fired contracts notwithstanding FERC's orders, the Third Circuit's decision in *NJBPU*, and the Supreme Court's decision in *Hughes*.

Second, if FERC is correct that states would continue to subsidize new renewable resources "with or without a renewables exemption," Remand Order P 62, JA____-__, then there is no reason to rescue states from their own policy choices by suppressing wholesale capacity rates paid to competitive merchant generators. FERC purports to be "balancing generators' and customers' interests." FERC Br. 55 (quoting Remand Rehearing Order P 43, JA ___). But FERC forgets it is state regulators, not generators, who are holding customers hostage. That is the correct way to examine the equities here and it is precisely why FERC and reviewing courts have refused to allow states to artificially suppress capacity prices in prior cases. *See, e.g.*, *NJBPU*, 744 F.3d at 97 (quoting *CTDPUC*, 569 F.3d at 481); *NESCOE*, 142 FERC ¶61,108 at P 34.

Third, FERC cannot purport to engage in rational decisionmaking, or pretend to "balance" factors relevant to its decision, when FERC fails to acknowledge one half the equation in a forthright manner. Petitioners have argued from the outset of this case that the renewable exemption is unjust, unreasonable, and unduly discriminatory because it is "a tool for transferring value from capacity sellers to capacity buyers by forcing the market-wide clearing price below the true cost of new entry." Pet'r Br. 35; *see* Remand Rehearing 29, JA____; Rehearing 17, JA____; NextEra Protest 11-12 & tbl. 1, JA____-__; Kalt Aff. 16:2-4, JA____; PSEG Protest 10-12, JA____-__. After ignoring that argument in its first set of

orders, FERC held on remand that competitive generators are not actually "paying for" the renewable exemption at all, but are merely being forced to accept a lower market price caused by "state policy mechanisms." Remand Rehearing Order P 46, JA____-__. On review, FERC perpetuates this fiction by claiming "[t]here is no actual dispute that the costs are ultimately paid by consumers." FERC Br. 37; *accord* Int. Br. 27-28. That is a misleading *non sequitur*. Yes, consumers ultimately pay for capacity charges passed through in retail rates, but this case is about who pays for the *exemption*. And here, "[i]t is beyond legitimate dispute that all uneconomic entry causes sellers to pay for out-of-market supplies by lowering market prices." Pet'r Br. 36-37 (citing, as examples, *NEPGA*, 757 F.3d 283 at 294, and *PJM Interconnection, L.L.C.*, 128 FERC ¶61,157 at P 90). FERC cannot answer that objection by continuing to quibble that the exemption does not cause generators to "pay" for anything. *See* FERC Br. 41.

III. FERC'S DELIBERATE ACCOMMODATION OF ARTIFICIAL PRICE SUPPRESSION THROUGH THE RENEWABLE EXEMPTION IS NOT THE PRODUCT OF REASONED DECISIONMAKING

FERC argues that the deliberate price suppression caused by the renewable exemption was acceptably "limited" to some unidentified degree by a sloped demand curve, a 200 MW annual limit based on ISO-NE's load growth projections, and anticipated retirements. *See* FERC Br. 22-29. FERC acknowledges that neither ISO-NE nor FERC ever attempted to quantify the effect

those factors might have on capacity prices, but instead rested on Dr. Ethier's assertion that those factors should allow capacity prices to be "near" the net Cost of New Entry. *Id.* at 32. In FERC's view, Dr. Ethier's predictions constituted substantial evidence sufficient to support FERC's finding that the exemption was just and reasonable, *id.*, and FERC had no duty to determine how significant the price impact of the renewable exemption would be, *see id.* at 32-33. Neither of those claims is correct. The defects in FERC's reasoning were apparent on the face of the record before FERC issued its initial set of orders and those defects were glaringly visible on remand. Moreover, days before this brief was filed, ISO-NE explained that each statement in the paragraph FERC has continuously relied upon was incorrect. *See ISO New England Inc.*, Docket No. ER18-619, Transmittal Letter at 10-12 (Jan. 8, 2018).

A. FERC Cannot Rationally Set Rates Without Quantifying Price Effects

The FPA and the APA require FERC to assess the "end result" of its ratemaking decisions with some measurable degree of rough approximation. *See* Pet'r Br. 38-39 (citing *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Sierra Club v. FERC*, 867 F.3d 1357, 1374 (D.C. Cir. 2017), *reh'g pending*; *Ill. Commerce Comm'n v. FERC*, 576 F.3d 470, 477 (7th Cir. 2009); *La. Pub. Serv. Comm'n v. FERC*, 184 F.3d 892, 898 (D.C. Cir. 1999)). FERC's orders on remand vigorously "reject[ed] the implied assumption [it] must develop a bright line for

the amount of artificial price suppression that is or is not acceptable." Remand Order P 39, JA____. And FERC disagreed "that the only way to evaluate the justness and reasonableness of the renewables exemption is to quantify the potential price impact [its] policy decision has on suppliers." Remand Rehearing Order P 43, JA____. On review, FERC insists that judicial precedent "does not require precise quantification." FERC Br. 33 (citing cases).

FERC substitutes a straw man to distract from the real argument. Petitioners have clearly acknowledged that FERC "is not required to forecast rates with 'exacting precision.'" Pet'r Br. 39 (quoting *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1369 (D.C. Cir. 2004)). Our argument is that FERC's orders came nowhere near providing even a rough quantitative estimate of what the effect of its renewable exemption would be. *See id.* FERC cannot pretend to engage in reasoned decisionmaking when it does not even acknowledge the mathematical fact that the renewable exemption can only result in price suppression, repeating FERC's position below that price reduction is only a "potential" outcome. *E.g.*, FERC Br. 2, 15, 16, 18-19, 20, 22, 23, 24, 27, 40, 41, 51, 52. That posturing is absurd when FERC simultaneously continues to emphasize the express purpose of the exemption is to reduce capacity prices paid by consumers. *E.g.*, *id.* at 13, 17, 37, 38, 39, 48, 51, 55.

Vague assertions that FERC expects price suppression to be "temper[ed]," "mitigate[d]" or "limited," *e.g.*, Remand Order PP 28, 36, 39, JA____,____-__, ____, fall far short of FERC's duty to provide "a quantitative estimate" of the effects its orders will have or to explain "specifically why it could not have done so." *Sierra Club*, 867 F.3d at 1374.

B. A Sloped Demand Curve Does Not Justify Artificial Price Suppression

1. Unrebutted Record Evidence Demonstrates the Renewable Exemption Permits Significant and Continuing Artificial Price Suppression Under a Sloped Demand Curve

A central element in FERC's orders below was that a sloped demand curve would "help mitigate price suppression created by the renewables exemption." Remand Order P 46, JA____. Neither ISO-NE nor FERC attempted to estimate what that effect would be. The only quantitative evidence on that subject was submitted by Dr. Hunger and Mr. Schnitzer. Dr. Hunger demonstrated that 100 MW of exempt renewables in one year would suppress capacity revenues by 4% or $188 million; 200 MW would suppress revenues by 8% or $370 million; and 600 MW under the carry-forward provision would suppress revenues by 23% or $1.028 billion. Pet'r Br. 44 (citing NextEra Protest 12 & tbl. 1; Hunger Aff. ¶¶18-19, JA____-__; Rehearing 7, JA____). Mr. Schnitzer's analysis yielded very similar results. *See id.* (citing Schnitzer Aff. 6, JA____).

When confronted with this evidence, ISO-NE conceded that it had not attempted to quantify the effects of the renewable exemption because the exemption was proposed to stakeholders *after* the Brattle Group's economic analysis of ISO-NE's sloped demand curve proposal was completed. *See* ISO-NE Answer 16, JA____. Notwithstanding that concession, FERC ignored the existence of the evidence presented by Dr. Hunger and Mr. Schnitzer in its initial orders. *See* Pet'r Br. 46. On remand, FERC explained that it chose to proceed on the basis of Dr. Ethier's unsupported assertion that the renewable exemption would still permit capacity prices somewhere "near" the net cost of new entry. FERC Br. 28, 32; Remand Order P 40, JA____; Remand Rehearing Order P 44, JA____.

That was not reasoned decisionmaking and FERC cannot justify its original refusal to address this issue by recasting its orders as a reasoned choice between the "conflicting estimates" of expert witnesses "based on ISO-NE and petitioners making different assumptions about the steepness of the supply curve." Remand Order P 40, JA____; *see* Remand Rehearing Order P 37, JA____. FERC continues to press that fiction on review, *see* FERC Br. 28, but it is not true that Dr. Ethier "offered a cogent explanation for why the supply curve is likely to be flatter than those used by Generators' experts to evaluate the renewables exemption" or that ISO-NE "assumed a flatter, more realistic supply curve for its own analysis." *Id.* at 28, 29 (citing Remand Order P 40 (citing Ethier Test. 8-9, JA____-__)). The

testimony cited in the Remand Order was no rebuttal; it was prepared before Dr. Hunger and Mr. Schnitzer filed their testimony, which were submitted in protest to the absence of any quantification of the renewable exemption by ISO-NE. Nor is it true that ISO-NE employed a flatter supply curve: Dr. Hunger used ISO-NE's supply curve and Mr. Schnitzer used a flatter one. Pet'r Br. 47.

2. FERC's Post Hoc Attacks on the Record Evidence Fail

On remand, FERC claimed Petitioners' arguments proved "unrealistic" because the quantity of new renewable resources that entered under the exemption was significantly below the 200 MW annual cap. Remand Order P 44; *see* Remand Rehearing Order PP 6, 36-37, 73, 78, JA____, ____-__, ____, ____. Of course, it is cold comfort to competitive generators for FERC to defend its orders after the fact on the ground that those auction results could have been worse. FERC's orders overlook that the exemption's carry-forward provision poses a constant threat and that it takes time for states to develop and award contracts for new capacity in the full quantities the exemption allows. To date, 106 MW have entered the capacity market through the renewable exemption—which has cost the competitive generation sector $324.6 million—and 513 MW are permitted to enter through the carry-forward provision in the February 2018 auction. *See* 2017 CELT Report, *supra* note 1, Tab 4.2, RTR Allotments.

It is no accident that, emboldened by the exemption, New England states procured very large quantities of new renewable resources in 2017. *See* Pet'r Br. 48; Remand Rehearing 44, JA____. ISO-NE submitted the quantity of that capacity that will enter the next auction to FERC, under seal, in late November 2017. But whatever that number may be, ISO-NE has already indicated that it is not enough to meet the states' renewable energy targets. On January 8, 2018, ISO-NE filed a fundamentally new capacity market construct called Competitive Auctions with Sponsored Policy Resources, or "CASPR," because the current renewable exemption is insufficient to permit the entry of new "clean energy procurements in the range of 2,800 MW" required by state law. *ISO New England, Inc.*, Docket No. ER18-619, Transmittal Letter at 3-4 (Jan. 8, 2018).

C. Load Growth Does Not Justify Artificial Price Suppression

FERC accepted the 200 MW annual renewable exemption based on ISO-NE's forecast of average annual load growth. *See* Order P 83, JA ___; FERC Br. 24. Neither ISO-NE nor FERC has ever explained the basis for the 600 MW carry-forward provision. *See* Pet'r Br. 50; Rehearing 12, JA____; NEPGA Protest 17, JA____.

It has been clear from the outset of this case that ISO-NE's load growth estimates were too ambitious. *See* Rehearing 11, JA____. The evidence that wholesale load in New England was actually shrinking had become so clear when

this case was pending on review for the first time that Petitioners argued remand was required under *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 172 (1962). *See* Pet'r Br. 50-52. Nevertheless, after requesting a voluntary remand, FERC declined to reform any of its prior conclusions when it reacquired jurisdiction over this case. Confronted with even stronger evidence that load growth would continue to decline, as reflected in ISO-NE's downward adjustment of the Installed Capacity requirement, FERC conceded that "load growth in New England has been lower than expected." Remand Rehearing Order P 72, JA____. But FERC argued that the 200 MW exemption was still supported by "substantial evidence" because it "represented ISO-NE's best estimate of average annual load growth at the time it submitted the Demand Curve Changes filing in 2014." Remand Rehearing Order P 72, JA____. FERC argues the same thing again on review, claiming that "reasoned decisionmaking does not require complete prescience." FERC Br. 26 (quoting *Fla. Gas Trans. Co. v.* FERC, 604 F.3d 636, 645 (D.C. Cir. 2010)).

FERC's position has no merit because FERC took this case back on voluntary remand, at which time FERC was free to act upon incontrovertible evidence that an essential element of its reasoning was false. *See* Pet'r Br. 53. Petitioners are not aware of any precedent, and FERC *still* cites none, that permits a federal agency to rest its decision on information the agency knows is false at the

time the decision is made. *See id.* And FERC's silence on this score is difficult to ignore when FERC argues that it was appropriate to justify its initial orders on the basis of auctions that occurred after those were issued, stating that there is "no legal proposition that precludes the Commission's reliance on public records while the record remains open." FERC Br. 31. Voluntary remand is an empty and prejudicial exercise if FERC is permitted to cherry-pick the facts.

The 200 MW annual exemption is an arbitrary number if it is disconnected from load growth. That connection was essential to FERC's finding that the 200 MW exemption would cause "limited" price suppression. Dr. Ethier squarely conceded there will be "systematic downward pressure on prices" if "exempted renewable entry does not exceed average annual load growth." Pet'r Br. 45 (quoting Ethier Test. 41:3-5, JA____).

Finally, nothing in FERC's remand orders or FERC's brief on review answers Petitioners' objections "that it is indefensibly discriminatory and preferential for FERC to erase competition for new load," that this defeats "the most basic design objective" of the Forward Capacity market, and that this approach "merely reinstituted the error in ISO-NE's earlier Alternative Price Rule" identified in *NEPGA*. Pet. Br. 49.

D. Retirements Do Not Justify Artificial Price Suppression

When FERC's load growth rationale evaporated, FERC turned its emphasis to anticipated retirements and pretended this had always been a key feature in its reasoning. *See* Pet'r Br. 53-54. On review, FERC perpetuates this fiction by intertwining its discussion of retirements with load forecasts, leaving an impression the 200 MW annual cap was tied to both. *See* FERC Br. 24-27. That is revisionist history. FERC does not rebut Petitioners' observation that FERC's initial orders only mentioned retirements in passing one time each when those orders were paraphrasing a single sentence in Dr. Ethier's testimony. Pet'r Br. 54 (citing Order P 83, JA____; Rehearing Order P 21, JA____). Moreover, Dr. Ethier's assertion about anticipated retirements was as wrong as his prediction about load growth. He predicted 6,500 MW of retirements by 2020, Ethier Test. 41:14-17, JA____, but FERC itself acknowledged his prediction was 2,300 MW too high, Remand Rehearing Order P 73, JA____-__. That is a material error in a market that "needs to procure roughly 35,000 MW annually," but estimates ranging from "approximately 4,200-10,000 MW" in a market that size are apparently close enough for FERC's purposes when it takes a case back on remand. FERC Br. 26 (quoting Remand Rehearing Order P 81, JA ___).

In short, the 200 MW annual exemption limit was not tied to retirements, it was tied to load forecasts, and the Court should not allow FERC to swap those

rationales at will. Dr. Ethier only mentioned retirements to support his claim that there would still be a role for competitive resources under the exemption, stating that "merchant entry would be required to meet retirements" after competition for load growth had been set aside for state-sponsored renewables. Ethier Test. 41:15-16, JA____. FERC double-counts retirements in its orders on remand to serve two different purposes.

E. New Demand Curves Do Not Justify Artificial Price Suppression

While this case was pending on remand, FERC accepted new revisions to the demand curve that significantly increased the artificial price suppression caused by the renewable exemption. *See* Pet'r Br. 55-56. Petitioners explained that this change not only caused a new injury, but that FERC could not purport to accurately assess the effect of renewable exemption on remand without taking the new demand curve modification into account. *See id.* at 56. FERC brushes that argument aside as a mere "preference" about docket management. FERC Br. 32. It is not. The question presented in *this* antecedent case is whether FERC rationally considered the renewable exemption's price effects and *this* case was still live on remand at FERC's own request when FERC accepted significant changes to the demand curve. It was not reasoned decisionmaking for FERC to ignore those changes on remand.

F. ISO-NE Now Concedes The Only Evidence Supporting FERC's Orders Below Was Fundamentally Mistaken

Petitioners explained that FERC's orders in this case turn entirely on the validity of assertions made in a short passage of Dr. Ethier's testimony. *See* Pet'r Br. 40-42 (quoting Ethier Test. 41:10-17, JA____). ISO-NE has now filed an entirely new paradigm for operating its capacity market—the Competitive Auctions with Sponsored Policy Resources proposal—that specifically disavows the accuracy of the analysis FERC relied upon below. *See ISO New England Inc.*, Docket No. ER18-619, Transmittal Letter at 10-11 (Jan. 8, 2018).

ISO-NE states that, "In approving the [Renewable Technology Resource] exemption, the Commission relied on the ISO's assertion that the risk of market price suppression was acceptable, because it would be minimized by load growth, retirements, and the initial demand curve with which it was filed." *Id.* at 10. ISO-NE then inserts a block quote reproducing page 41 of Dr. Ethier's testimony in this case. *See id.* After doing so, ISO NE states that:

> Three years later, the ISO's expectations have not materialized, and the [Renewable Technology Resource] exemption now presents a greater risk of price suppression. Specifically, the region now has significant excess capacity; in [Forward Capacity Auction] 11, [the Forward Capacity Market] procured excess resources amounting to 1,760 MW over the net Installed Capacity Requirement ("NICR"). As a result, [the Forward Capacity Market] cleared well below the Net Cost of New Entry ("CONE") in [Forward Capacity Auction] 11. Exacerbating this situation, Massachusetts is expected to contract for approximately 2,800 MW (nameplate value) of sponsored *new* supply resources to meet legislative mandates, and the region has not

> experienced the expected load growth. On the latter point, for [Forward Capacity Auction] 12, [the net Installed Capacity Requirement] declined to 33,725 MW from 34,075 in [Forward Capacity Market] 11. There were small declines in [Forward Capacity Auctions] 9 and 10 as well. Under these conditions, the market may continue to clear well below [the Net Cost of New Entry] for the foreseeable future.

Id. at 11 (footnotes omitted).

ISO-NE explains that Forward Capacity Auction 11 cleared at $5.30 and the Net Cost of New Entry for Forward Capacity Auction 11 was $11.64. *Id*. n.34. As a result, "[t]he region would need retirements in the amount of more than 3,000 MW within a year to return to the point of clearing at a price level near the cost of new entry, where the [Forward Capacity Auction] might again attract competitive new supply." *Id.* n.37. ISO-NE concludes these "changed market conditions" require "elimination of the [Renewable Technology Resource] exemption" and rejects the states' request for a guaranteed exemption each year because "such guarantees are antithetical to competitive markets." *Id*. at 12. However, "ISO recognizes that abrupt changes to existing market rules can have adverse impacts on investments that are already underway." *Id.* To "minimize such adverse effects," ISO-NE proposes "to phase out the [Renewable Technology Resource] exemption by allowing accrued exempt MWs (currently 514 MW) to be used through [Forward Capacity Auction] 15, to be conducted in 2021." *Id.* at 12-13.

CONCLUSION

For the reasons set forth above, the petition for review should be granted.

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January 11, 2018

CERTIFICATE AS TO LENGTH OF BRIEF

Pursuant to Rule 32(a)(7)(B) of the Federal Rules of Appellate Procedure, I hereby certify that the foregoing document contains no more than 7,800 words (XXX words using the word-count feature in Microsoft Word) not including the tables of contents and authorities, glossary, and certificates of counsel.

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CERTIFICATE OF SERVICE

Pursuant to Rule 25(d) of the Federal Rules of Appellate Procedure and Rule 25(c) of the Circuit Rules of this Court, I hereby certify that on January 11, 2018, I electronically filed the foregoing document with the Clerk of the Court for the United States Court of Appeals for the District of Columbia Circuit by using the CM/ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

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