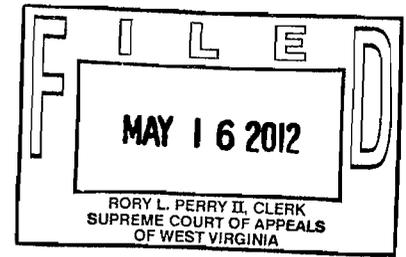


IN THE SUPREME COURT OF APPEALS
OF WEST VIRGINIA
CHARLESTON



Morgantown Energy Associates,
Petitioner

vs.) No. 11-1739

Public Service Commission of West Virginia; Monongahela Power Company and The Potomac Edison Company, both dba Allegheny Power,
Respondents

And

City of New Martinsville,
Petitioner

vs.) No. 11-1738

Public Service Commission of West Virginia; Monongahela Power Company and The Potomac Edison Company, both dba Allegheny Power,
Respondents

SUPPLEMENTAL BRIEF OF THE PUBLIC SERVICE COMMISSION

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May 16, 2012

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SUPPLEMENTAL BRIEF OF THE PUBLIC SERVICE COMMISSION

I. STATEMENT OF THE CASE

By Order entered May 1, 2012, this Court determined that supplemental briefs should be filed addressing the impact of the FERC Order entered on April 24, 2012, including the extent to which additional PSC proceedings were necessary prior to the Court's resolution of the appeals.

The PSC Order stated three bases, founded in state law, for its decision that the utilities owned the credits associated with the generation. Because these have been previously argued to this Court, those bases can be briefly summarized as (1) consistency with the intent of the Portfolio Act, (2) the unqualified utility ownership of the electricity when the credits are created and (3) the provisions of Chapter 24 of the West Virginia Code that require the PSC to balance

interests, consider equity and assure reasonable utility rates. PSC Order at 43 (discussed at 28-34).

The FERC Order chose to ignore the stated bases of the PSC Order and provided its own rationale for the PSC decision. Contrary to FERC's analysis, the PSC Order did not determine that the avoided cost rate in the PURPA contract conveyed the RECs. The PSC Order did not determine that there was any conveyance of credits. Rather, as explained in the PSC Order, the utilities own the credits when they are created.

For these reasons, as more fully described below, the PSC respectfully submits that the FERC Order has no impact upon this appeal, no further PSC proceedings are required and that the Court should proceed with resolution of the appeals by affirming the PSC Order.

Relief Sought at FERC

On February 28, 2012 and on March 15, 2012, MEA and New Martinsville filed motions to defer oral argument that attached their respective petitions to FERC for a federal enforcement action based on alleged violations of PURPA. The lack of import of the FERC Order can be demonstrated by comparing the relief sought in the petitions filed by MEA and New Martinsville with the FERC decision.

In its petition to FERC, MEA alleged that the PSC Order violated PURPA in three respects. MEA asserted that the PSC Order violated PURPA because the PSC Order determined that the utility payment of an avoided cost rate was sufficient consideration to transfer the RECs from MEA to the utility; violated PURPA by unlawfully regulating the management practices of MEA; and violated PURPA by discriminating against MEA solely because of its QF status. MEA Motion of February 28, 2012, Exhibit B at 2. As relief, MEA requested that FERC bring

an enforcement action against the PSC or to declare that the PSC Order “violated the PURPA on the three issues identified” in its petition. *Id.* at 39.

New Martinsville alleged in its petition that the PSC Order constituted a rule that violated FERC decisions that the avoided cost rate in a PURPA contract does not compensate a QF for the environmental attributes of the generation; constituted a *post hoc* adjustment to the avoided cost rate that violated the Freehold¹ decision; and, discriminated against QFs. New Martinsville Motion of March 15, 2012, Exhibit B at 17. Like MEA, New Martinsville requested that FERC initiate an enforcement action against the PSC in federal court or issue an order that is a clear statement as to the lawfulness of the challenged order. *Id.* at 42.

FERC Decision

In its April 25, 2012 letter to the Court, MEA was quick to declare victory based upon the concluding paragraph of the April 24, 2012 FERC Order “that the West Virginia Order is inconsistent with PURPA and the Commission’s regulations as discussed in the body of the order.” A review, however, of the FERC order reveals either FERC’s confusion or a misunderstanding of the bases of the PSC Order. The FERC actually denied the primary relief sought by the petitioners. Specifically, the FERC Order denied the mutual requests of MEA and New Martinsville that FERC initiate an enforcement action in federal district court. Furthermore, FERC failed to provide the requested “clear statement” as to the lawfulness of the PSC Order by declining to reach any conclusion regarding the alleged violations of PURPA. The FERC Order made no determination about the alleged impermissible management of the QF, the alleged *post hoc* reduction of the avoided cost rate or the asserted discrimination against the QFs.

¹ Freehold Cogeneration Assocs., L.P. v. Bd. Of Regulatory Commissioners of N.J., 44 F.3d 1178 (3rd. Cir. 1995)

The FERC Order equivocated by characterizing certain statements within the PSC Order as “inconsistent” with PURPA rather than reaching the conclusion sought by the petitioners that the Order violated PURPA. That FERC ordering paragraph directed the reader to the body of the FERC order for discussion as to how the PSC Order was “inconsistent” with PURPA. The last sentence of the first paragraph stated that “as discussed below, we conclude that certain statements in the West Virginia Order are inconsistent with the requirements of PURPA.” Other than this bald conclusory statement, the first 44 paragraphs of the FERC Order, except paragraph 9, are straight forward recitals of the PSC proceeding, the FERC proceeding, a summary of the various assertions of the parties to the FERC proceedings and a summary of the enforcement provisions. In paragraph 9, FERC ignored the stated bases of the PSC Order and substituted its own conclusions concerning the reasons for the decision including the misstatement that the PSC Order credits are created simultaneously with the generation of electricity.

In paragraph 45, FERC determined that it would not go to court to seek enforcement, and it footnotes that statement with the observation that its decision not to go to Court effectively mooted the PSC claim that the petition was not appropriately before the FERC in the first instance.² FERC concluded paragraph 45 with the statement that, although it is not going to seek enforcement, it finds that “certain statements in the West Virginia Order are inconsistent with PURPA.” In the following paragraph 46, FERC briefly recited its holding in American Ref-

² The PSC advanced the same argument to FERC that is contained in the PSC’s Response to the Motions to Continue Oral Argument filed with this Court on March 9, 2012. First, the PSC argued that its order had no effect upon PURPA or the contracts between MEA, New Martinsville and the utility. But, if there was an effect, it did not involve “implementation” of PURPA. Rather, the effect would be a challenge of a PSC action “as applied” to the QFs, Therefore, the challenges are specifically reserved to the state courts, not federal courts. Power Res. Grp. v. Public Util. Commission of Texas, 422 F.3d 231, 235 (5th Cir. 2005), cert. denied, 547 U.S. 1020, 126 S.Ct. 1583, 164 L.Ed.2d 301 (2006); 16 U.S.C. 824a-3(g).

Fuel³ (much discussed in the Commission Order and the briefs to this Court) for the proposition that the sale of QF power does not convey RECs to the purchasing utility.

In paragraph 47, the FERC concluded its discussion of American Ref-Fuel by stating that “To the extent that the West Virginia Order finds that avoided-cost rates under PURPA also compensate for RECs, [footnote 68], the West Virginia Order is inconsistent with PURPA.” In footnote 68, the FERC erroneously stated that the PSC Order primarily relied on the avoided cost rates in the PURPA contracts to justify that the RECs produced by the QFs are owned by the utility in the first instance and referenced the PSC Order at 28-31. FERC states:

“For example, the West Virginia Order states that avoided cost rate contracts under PURPA provide a substantial consideration to the QF sufficient to compensate not only for the energy and capacity contemplated in those contracts, but also for the RECs produced by the QFs. See West Virginia Order at 28.”

There is no other discussion in the FERC Order finding “inconsistencies” with PURPA.

II. SUMMARY OF ARGUMENT

Twice in its Order, FERC indicated that certain statements in the West Virginia Order are inconsistent with PURPA. Paragraphs 1 and 45. The FERC characterization of certain statements as inconsistent cannot be construed as a determination that PURPA has been violated or that the PSC has failed to implement FERC PURPA regulations. The FERC Order made no determination that the PSC Order is unlawful in any respect. The FERC Order cannot support the conclusion that the state law bases of the PSC Order are incorrect.

Contrary to FERC’s interpretation, the PSC Order did not hold that the credits were transferred from the QF to the utilities. The PSC Order concluded, after applying state law, that the utilities own the credits in the first instance.

³ American Ref-Fuel Company, 105 FERC ¶ 61,004 (2003)

The FERC Order is of “no legal moment” and is of no legal value in resolving the pending appeals. Since the PSC did not determine that the credits “transferred,” the FERC Order does not require further proceedings before the PSC. The PSC respectfully requests that this Court proceed with the resolution of these appeals by affirming the PSC Order.

III. ARGUMENT

The FERC Order Misconstrues the PSC Order

The PSC Order stated three bases, founded in state law, for its decision that the utilities own the credits associated with the generation. Because these have been previously argued to this Court, those bases can be briefly summarized as (1) consistency with the intent of the Portfolio Act, (2) the unqualified utility ownership of the electricity when the credits are created and (3) the provisions of Chapter 24 of the West Virginia Code that require the PSC to balance interests, consider equity and assure reasonable utility rates. PSC Order at 43 (discussed at 28-34).

The FERC Order chose to ignore the stated bases of the PSC Order and provided its own rationale for the PSC decision. Contrary to FERC’s analysis, the PSC Order did not determine that the avoided cost rate in the PURPA contract conveyed the RECs. There is simply no such statement. The FERC Order referenced page 28 of the PSC Order for such a statement. There is no such statement on page 28. Page 28 involved a discussion in response to the arguments of MEA and New Martinsville that PSC Rules 5.2 and 5.6 were dispositive of the ownership issue. On page 28, the PSC explained that those rules would not apply to the projects of MEA and New Martinsville for the reasons that (i) the rules were intended to apply prospectively to projects which would address credit ownership in contracts; (ii) the projects were constructed well in advance of the advent of credits; and (iii) the projects were constructed pursuant to the incentives

provided by PURPA (entitlement to avoided cost rate and utility obligation to purchase) as well as the benefits contained in the contracts approved by the PSC. Nowhere on page 28 of the PSC Order does the statement exist that the PURPA avoided cost rate was adequate consideration for the transfer of the RECs from the QFs to the utility.

The FERC conclusion that there has been a transfer of the RECs is FERC's "interpretation" of the PSC Order, rather than an acknowledgment of the plain language of the PSC Order itself. No clearer statement could exist than that in the PSC Order:

"In the instant case, moreover, there is no property right that has been 'taken' from the QFs because the QFs never owned the credits. As we have determined, the QFs have sold the electricity and Mon Power has an obligation to take the electricity as it is generated, which is also when the credits are created. Therefore, the QFs do not own the electricity at the time the credits are created, and, therefore, do not possess a property right in the credits. The credits cannot be taken from the QFs when the credits do not rightfully belong to them when they are created."

PSC Order at 40.

The FERC Order misconstrued not only the PSC Order but also the state law. Rather than properly acknowledging the plain language and bases of the PSC Order, FERC stated in paragraph 9 of its order that there are eight reasons (not the three bases identified by the PSC Order) for the PSC concluding that the utility owned the credits. Reason 8 given by the FERC for the PSC decision is the PSC determination that "RECs are created simultaneously with electricity energy." The PSC Order did not use the term "simultaneously" because a credit under state law is not created "simultaneously" with the generation of the electricity. As emphasized several times in the PSC Statement of Reasons, under state law a credit exists only after one megawatt hour of generation has occurred. W.Va. Code §24-2F-4(b)(1). When the credit is created, the utility is the owner of the electricity. This fact, coupled with the observations that the PURPA contracts, executed well in advance of the advent of state credits, are necessarily

silent as to credits and that the QFs did not reserve any interest, present or future, in the electricity sold, formed one of the bases of the PSC Order.

The FERC Order Has No Legal Significance

Regardless of the FERC Order “determination” of the lawfulness of the PSC Order, the United States Circuit Court of Appeals has already determined that a FERC Order like this one is of no legal moment. When the FERC issued its decision in American Ref-Fuel, which involved a petition seeking enforcement pursuant to section 210(h) of PURPA like the petitions filed by MEA and New Martinsville, one of the parties to that proceeding filed an appeal of the FERC Order with the United States Court of Appeals for the District of Columbia Circuit. The Court determined that it lacked jurisdiction to entertain the appeal because the actual enforcement action in federal district court had not been taken and a final court order had not been issued. The Court of Appeals explained that:

“An order that does no more than announce the Commission’s interpretation of the PURPA or one of the agency’s implementing regulations **is of no legal moment** unless and until a district court adopts that interpretation when called upon to enforce the PURPA.’ *Niagara Mohawk Power Corp. v. FERC*, 326 U.S. App. D.C. 135, 117 F.3d 1485, 1488 (D.C. Cir. 1997[***5] Here, as in several other petitions for review we have refused to consider, ‘the Commission has in effect merely announced the position it would take in any future enforcement action that [Xcel] might bring.’ *Connecticut Valley Elec. Co. v. FERC*, 341 U.S. App. D.C. 68, 208 F.3d 1037, 1043 (D.C. Cir. 2000). The FERC position is reviewable by this court only after someone - a utility, a QF, or the Commission - brings an enforcement action in the district court and appeals therefrom. See *Industrial Cogenerators v. FERC*, 310 U.S. App. D.C. 357, 47 F.3d 1231, 1234 (D.C. Cir. 1995).”

Xcel Energy Services Inc. v. Federal Energy Regulatory Commission, 407 F.3d 1242, 1244

(D.C. Cir. 2005) (emphasis added).

The FERC Order should have no legal significance to this Court. Furthermore, the FERC Order has no value of persuasion given that it has ignored the stated bases of the PSC Order, has

misstated the bases of the PSC Order, failed to initiate a FERC enforcement action and contained no findings regarding violations of PURPA (only that certain statements in the PSC Order are inconsistent with PURPA), failed to make any findings regarding most of the QF claims, and failed to indicate which FERC regulations have not been implemented by the PSC.⁴ It should not be acknowledged as persuasive in any manner. Furthermore, FERC has attempted to finesse the PSC argument that an enforcement action is improper, not by pointing to a violation of FERC regulations, but rather by declaring the issue moot because FERC is declaring that it does not intend to bring an enforcement action. FERC Order at fn 61.

The FERC Order does not affect the legitimacy of the PSC argument in its Statement of Reasons that its Order did not affect the PURPA contracts and did not violate the holding in Freehold. The PSC Order determined the ownership of RECs. That is simply not a PURPA issue. In this regard, the PSC Order is the same as other state decisions that have determined the utility owns the credits. As stated by the Commonwealth Court of Pennsylvania,

“the Commission has not modified the terms of an existing and approved contract, but rather has determined ownership of assets which were not contemplated, let alone provided for in the contracts at issue.”

ARIPPA v. Pa. PUC, 966 A.2d 1204, 1210 (2007).

Indeed, FERC has acknowledged that PURPA does not control the issue of REC ownership. It is an issue outside of PURPA and controlled by state law. American Ref-Fuel, FERC Order, paragraph 46. *See*, Wheelabrator v. State of Connecticut Department of Public Utility Control, 526 F. Supp. 2d 295, 305-306 (D. Conn. 2006). Yet, FERC persists, for reasons that are not particularly clear, to state that certain statements within the PSC Order are

⁴ The federal statute provides for an enforcement action in federal district court when a state regulatory commission has failed to implement FERC PURPA regulations. 16 U.S.C. §824a-3(f) and (h).

inconsistent with PURPA.⁵ The FERC statement that the PURPA avoided cost rate does not convey the credit obviously does not resolve the issue of REC ownership. Every court that has considered the FERC statement (first stated in American Ref-Fuel) has declined to use the FERC statement as a basis for reversing a decision of a state regulatory commission which has determined that the utility owned the credits associated with vintage PURPA projects. ARRIPA v. Pa. PUC, *Supra*, 1209 (FERC has acknowledged that RECs are created by the states; they “exist outside the confines of PURPA,” and, therefore, PURPA does not address ownership of the credits); Wheelabrator v. Conn. Dep’t of Pub. Util. Control, 531 F.3d 183, 190 (2nd Cir. 2008) (FERC has determined that state law governs the conveyance of RECs, and that Congress has not demonstrated an intent to regulate such credits under federal law, therefore, there is no federal preemption of the issue); Wheelabrator v. Conn. Dep’t of Pub. Util. Control, 526 F.Supp. 2d 295, 305 (D. Conn. 2006) (the FERC concluded that RECs are created by the state and controlled by state law, not PURPA); In the Matter of the Ownership of Renewable Energy Certificates, 389 N.J. Super. 481, 913 A.2d 825, 831 (2007) (regardless of the discussion in American Ref-Fuel, the FERC determined that states decide who owns the REC in the initial instance). The Supreme Court of Connecticut addressed the FERC declaration by observing that

“We recognize that this conclusion [that the avoided cost rate itself was intended to provide an incentive to develop renewable energy sources] arguably is inconsistent with the conclusion of the federal commission in *In Re Covanta Energy Group*, *supra*, 105 F.E.R.C. 61,007 [American Ref-Fuel], that avoided costs were not intended to include the renewable attribute of the energy under federal law. We note, however, that the federal commission was split on that issue, that portion of the decision has been subject to some criticism; see E. Holt, R. Wiser & M. Bolinger, *supra*, p. 51; the only state court to confront the issue before this court declined to follow the federal commission’s decision, see *In re Ownership of Renewable Energy Certificates*, *supra*, 389 N.J. Super. 490-491; and the federal commission’s decision appears to be inconsistent with the United States Supreme Court’s determination that the avoided cost scheme was intended

⁵ Legally, the FERC could have issued no order, and after sixty days, MEA and New Martinsville could have initiated a federal district court action. 16 U.S.C. §824a-3(h)(2)(B).

to provide an incentive to develop renewable energy sources. *American Paper Institute, Inc. v American Electric Power Service Corp., Supra*, 461 U. S. 406.”

Wheelabrator v. Dep't. of Public Utility Control, 283 Conn. 672, 931 A.2d 159, 175, fn 25 (2007) (material in brackets not in original).

FERC cannot escape the legal reality that the determination of the ownership of RECs must be made under state law and is outside the purview of PURPA. Given FERC's misconstruction of the PSC Order, or its own deliberate reconstruction of the bases of the PSC Order rather than its plain language, the FERC Order is not only “of no legal moment,” but it cannot be deemed instructive to this Court. The FERC Order fails to identify how the actual PSC decision has violated PURPA or failed to implement FERC PURPA regulations.

IV. CONCLUSION

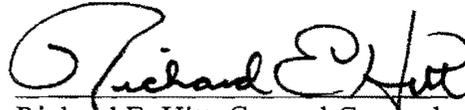
This matter is properly before this Court, including the PURPA issues. The PSC Order determined ownership of credits and did not involve a modification or change to the PURPA contracts. The only statements within the PSC Order that represented an inconsistency with PURPA, in FERC's opinion, was the extent to which the PSC determined that the avoided cost rate in the PURPA contracts conveyed the credits. Because the PSC made no such determination, there would be no reason for the PSC to reconsider its order. In fact, the PSC determined that the QFs never owned the credits, thus, there could be no transfer.

This case has been fully briefed, argued, and the issue represents millions of dollars in potential costs to the West Virginia ratepayers of Monongahela Power and Potomac Edison. The PSC respectfully requests that the Court proceed with the resolution of these appeals by affirming the decision of the Commission.

Respectfully submitted this 16th day of May 2012.

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

By Counsel

A handwritten signature in black ink, appearing to read "Richard E. Hitt". The signature is written in a cursive style with a large initial "R" and "H".

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CERTIFICATE OF SERVICE

I, Richard E. Hitt, General Counsel for the Public Service Commission of West Virginia, do hereby certify that copies of the foregoing Supplemental Brief has been served upon the following counsel of record via First Class United States Mail Postage Prepaid on this 16th day of May, 2012:

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