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May 10, 2012

The Honorable Martin O'Malley
Governor of Maryland
State House
100 State Circle
Annapolis, Maryland 21401-1991

Re: House Bill 1186 and Senate Bill 652

Dear Governor O'Malley:

We have reviewed House Bill 1186 and Senate Bill 652, identical bills titled "Renewable Energy Portfolio Standard – Renewable Energy Credits – Geothermal Heating and Cooling," for constitutionality and legal sufficiency. While we approve the bills we note that a severable portion may violate the Commerce Clause of the United States Constitution.

Under Maryland's renewable energy portfolio standard (RPS) program, a certain percentage of electricity sold at retail in the State must come from either Tier 1 or Tier 2 renewable sources. The program is implemented through the creation, sale or transfer of renewable energy credits (RECs). A REC is equal to the generation attributes of 1 megawatt hour of electricity produced from a Tier 1 or Tier 2 renewable source, as defined in the RPS statute. RECs are obtained by generating electricity from Tier 1 or 2 renewable sources or by purchasing or otherwise obtaining REC's from Tier 1 or Tier 2 renewable sources or suppliers. To be eligible to meet the Maryland RPS standard, Tier 1 and Tier 2 renewable sources must be located in the PJM region or in a control area that is adjacent to the PJM region if the electricity is delivered into the PJM region. However, as discussed below, this geographic limitation has been further narrowed by legislation in recent years for certain Tier 1 renewable sources, including solar, poultry litter-to-energy, waste-to-energy, and refuse derived fuel.

Since the initial enactment of the Renewable Portfolio Standards Act, Chapter 487, Laws of 2004, the Office of Attorney General has examined the constitutionality of qualifying renewable energy credits. Limitations imposed by the statute narrow the geographical area from which credits may qualify to meet energy suppliers' RPS requirement. House Bill 1186 and Senate Bill 652 add geothermal heating and cooling pumps to RPS resources, but they must be "connected to the distribution grid serving Maryland" to count toward meeting the State's RPS. There is an interstate market for renewable energy credits and imposing geographical limits on renewable energy credits may interfere with interstate commerce. Although the size of the impact that will be attributable to ground water heating and cooling pumps is not determinable at this time and could be minimal, it is possible a court would find that the bills, in part, violate the Commerce Clause of the United States Constitution.

Under Maryland law, energy is eligible for inclusion in the renewable energy portfolio standard only if it comes from a source located in the PJM region or in a control area that is adjacent to the PJM region, if the electricity is delivered into the PJM region. Public Utilities ("PUC") Article § 7-701(i). The PJM region is the control area administered by the PJM Interconnection, Inc., and currently includes all or parts of Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and the District of Columbia.[1] Some Tier 1 sources are subject to the further requirement that the source be "connected with the electric distribution grid serving Maryland." PUC § 7-704(a)(2)(i)1. Distribution grids are not necessarily interstate systems, but are usually thought of as a small voltage component of the electric grid (a portion of the electric grid serving a discrete area such as a residential neighborhood or commercial area) as opposed to a transmission system which usually serves to transfer larger voltages between the point of generation and interim substations. The intent of the "connected with the electric distribution grid serving Maryland" language appears to be to give favorable treatment only if the facility is located in Maryland or possibly adjacent to Maryland because of the requirement that it be connected to the distribution system serving Maryland. It is possible that some out-of-state sources may be connected to the distribution grid serving

[1] In the Bill Review Letter on House Bill 1308 and Senate Bill 869 of 2004, which adopted the renewable source portfolio standard, we concluded that while those bills on their face appeared to discriminate against some interstate commerce, the practical effect would be minimal because, "under the regional system developed by FERC, most of the electricity consumed in the State is generated within the PJM region, and very little is produced in states that are the farthest away." We can continue to hold this view.

Maryland, but, as a practical matter, they must be located fairly close to the borders of the State.[2]

The Commerce Clause of the United States Constitution, Article I, § 8, cl. 3, provides that "The Congress shall have Power ... To regulate Commerce with foreign Nations, and among the several States and with the Indian tribes." Although it is stated as a grant of power to Congress, it has long been recognized that the Commerce Clause has a dormant aspect that "prohibits States from 'advancing their own commercial interests by curtailing the movement of articles of commerce, either into or out of the state." *Fort Gratiot Sanitary Landfill v. Michigan*, 504 U.S. 353, 359 (1992). Thus, "where simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected. ... But where other legislative objectives are credibly advanced and there is no patent discrimination against interstate trade, the Court has adopted a much more flexible approach." *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978). The sale of electrical power across state lines is commerce among the several states within the meaning of the Commerce Clause. *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927).

In *Wyoming v. Oklahoma*, 502 U.S. 437 (1992), the Supreme Court found that an Oklahoma law requiring coal-fired electric generating plants in the state to burn a mixture of coal containing at least 10% Oklahoma-mined coal violated the Commerce Clause. Noting that *New Energy Company of Indiana v. Limbach*, 486 U.S. 269, 273 (1988) had held that the "negative" aspect of the Commerce Clause prohibits economic protectionism, "that is, regulatory measures designed to benefit in-state economic interests by burdening our-of-state competitors," the Court found that the 10% requirement discriminated against out-of-state commerce and was invalid. In doing so, the Court rejected arguments that the statute should be upheld because the burden on commerce was de minimis, stating that the "volume of commerce affected measures only the extent of the discrimination; it is of no relevance to the determination of whether a State has discriminated against interstate commerce." *Id.* at 455. Because the act discriminated against interstate commerce, the Court applied the strictest scrutiny and found that the state had failed to meet its burden to "justify [the discrimination] both in

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[2] The Bill Review Letter on Senate Bill 595 and House Bill 1016 of 2007 found that this limitation did not violate the Commerce Clause as applied to solar energy, noting that "virtually all solar power is produced by customer-generators who install solar generating systems for their own energy needs and sell the excess to their own electric company," and that "technical barriers exist to importation of solar energy from out-of-state."

terms of the local benefits flowing from the statute and the unavailability of nondiscriminatory alternatives adequate to preserve the local interests at stake." *Id.* at 456.

As set forth in PUC § 7-704 (a)(2), solar, poultry litter, waste-to-energy facilities, and refuge-derived energy facilities must be connected with "the distribution grid serving Maryland" for the renewable energy credits generated by them to be counted meeting the State's renewable portfolio standard. As distribution grids are not interstate systems, the language creates the possibility of commercial balkanization. House Bill 1186 and Senate Bill 652 add geothermal heating and cooling systems to the list of Tier 1 facilities that must be connected with the distribution system serving Maryland but which sell no electricity to the grid. Because renewable energy credits are a commodity marketed to, and purchased by, energy suppliers that must meet the State's renewable portfolio standards, geographic limitations may impose impermissibly upon interstate commerce.

On their face, House Bill 1186 and Senate Bill 652 do not explicitly forbid the use of out-of-state sources or require the use of in-state sources. The bills do not prohibit any electricity supplier from purchasing electricity, renewable or otherwise, from any state in the country. They do not prohibit the sale in Maryland of electricity from any other state in this State. Moreover, it is possible under House Bill 1186 and Senate Bill 652 to meet the renewable energy portfolio standard using energy from out-of-state. Nevertheless, a Commerce Clause issue is raised, however, because the bill draws a distinction between some energy generated inside the State and most energy generated anywhere else for purpose of qualification for inclusion in the renewable energy portfolio standard. It also appears to prohibit certain types of out-of-state renewable energy sources, including geothermal heating and cooling systems, that are not connected to the distribution grid serving Maryland, from being able to sell their RECs to Maryland energy suppliers to meet the suppliers' RPS requirement. In other words, out-of-state renewable energy sources not connected to the distribution grid serving Maryland would be excluded from participating in the RPS market, whereas the same type of Maryland-located renewable sources connected to the distribution grid, would be allowed to participate in the RPS market.

In this instance, the ground water heat pump is a heating and cooling system, not a generation facility. In addition, it may not sell electricity to the grid, but is likely a small unit serving individual or multifamily residences and commercial buildings. Public Utilities Article §7-701(c-1)(6). The language requiring the system to be connected to an electric distribution grid in Maryland only serves to qualify the origin of the renewable energy credit that may be applied to the State's RPS. The magnitude of the impact of this new source of renewable energy credits will be dependent upon the number and size of units ultimately qualifying for Tier 1 resources, but credits generated by similar units located in adjacent states will not qualify to satisfy the State's RPS unless such sources are found to be connected to the distribution grid serving Maryland. Thus, the bills create an incentive for the purchase of RECs generated in or very near this State. Such "encouragement" of the use of in-state energy has been found to violate the Commerce Clause even where a law does not explicitly forbid the use of out-of-state sources or require the use of in-state sources. *Alliance for Clean Coal v. Bayh*, 72 F.3d 556, 560 (7th Cir. 1995) (economic incentives to use high-sulfur coal from in-state); *Alliance for Clean Coal v. Miller*, 44 F.3d 591 (7th Cir. 1995) (favorable treatment of use of in-state coal and requirement that large suppliers install scrubbers to allow the continued use of in-state coal).

To date, there are no reported cases on in-state energy requirements or limitations in the context of renewable energy portfolio standards. Commentators have generally agreed, however, that exclusion of out-of-state sources of renewable energy violate the Commerce Clause. Carolyn Elefant and Edward A. Holt, *The Commerce Clause and Implications for State Renewable Portfolio Standards Programs*, Webinar presented for Clean Energy States Alliance (Mar. 29, 2011);[3] Nathan E. Endrud, *State Renewable Portfolio Standards: Their Continued Validity and Relevance in Light of the Dormant Commerce Clause, The Supremacy Clause, and Possible Federal Legislation*, 45 Harv. J. Legis. 259, 271 (Winter 2008); Patrick R. Jacobi, *Renewable Portfolio Standard Generator Applicability Requirements: How States Can Stop Worrying and Learn to Love the Dormant Commerce Clause*, 30 Vt. L. Rev. 1079, 1082, 1111 (2006); Nancy Rader and Scott Hempling, *Renewables Portfolio Standard: A Practical Guide*, prepared for the National Association of Regulatory Utility Commissioners, Appendix A (2001).

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[3] *See* www.cleanenergystates.org/assets/Uploads/HoltElefantCommerce-Clause-110329.pdf (last visited May 8, 2012).

If a court finds that the limitation to sources connected to the Maryland grid is unconstitutional, our view is that that provision would most likely be found to be severable. Maryland law expressly provides for severability. Maryland Code, Art. 1, §23. Moreover, where a provision of a bill is found to be unconstitutional, it is generally presumed, "even in the absence of an express clause or declaration, that a legislative body generally intends its enactments to be severed if possible." *Davis v. State*, 294 Md. 370, 383 (1982). Thus, "when the dominant purpose of a statute may largely be carried out notwithstanding the invalid provision, courts will ordinarily sever the statute and enforce the valid portion." *Id.* at 384. It is clear that the purpose of the bill can be accomplished without the limiting language. As a result, it is our view that, if the limitation were to be found unconstitutional, it would be severable from the remainder of the bill.

Very truly yours,

Douglas F. Gansler
Attorney General

DFG/SBB/kk

cc: The Honorable John P. McDonough
Joseph Bryce
Karl Aro