State Power Project: Policymaker Summary

Addressing the Regulatory Holdout Problem in the Siting of Interstate Transmission Lines

Policymaker Summary of: Alexandra B. Klass and Jim Rossi, Revitalizing Dormant Commerce Clause Review for Interstate Coordination, Minnesota Law Review (forthcoming 2015)[1]

Key Takeaways:

Issue: Building new high-voltage electric transmission lines is essential for maintaining reliability and integrating large-scale renewable energy projects. Each state controls the process for approving and siting the electric transmission lines within its borders. Projects spanning multiple states require the approval of each state, allowing a single state to halt a multi-state project.

Challenge: Public utility and property laws that govern the electric transmission line siting and construction process are often aimed at protecting in-state interests. While these laws address many valid local concerns, they can be overly broad or applied in a manner that inhibits approval and siting of interstate transmission lines that produce regional benefits. State siting laws and practices are particularly problematic when:

1) out-of-state companies are prohibited from constructing projects or using eminent domain authority;
2) regulators narrowly frame a line's benefits when determining whether there is a "need" for the project; or
3) eminent domain authority is limited to projects that meet restrictive definitions of "public use."

Such laws or practices authorize regulators in a single state to exclude out-of-state entities from the siting process and prevent a project based on parochial concerns. These regulatory holdouts may serve to protect in-state property interests, and can provide leverage for bargaining that is ultimately beneficial. However, many of these policies and procedures also can inhibit the development of energy infrastructure and violate the dormant Commerce Clause. This constitutional doctrine prevents a state from discriminating against out-of-state economic interests, regulating out-of-state transactions,[2] or unduly burdening interstate commerce.

Recommendations: State legislatures should examine statutes governing approval of transmission lines as well as laws about eminent domain. State regulators should also assess their practices under existing statutes that delegate discretion to them. To facilitate better regional coordination and to avoid dormant Commerce Clause violations:

1) siting laws and procedures should allow out-of-state transmission line companies to apply for siting certificates and eminent domain authority and otherwise participate in proceedings about transmission on the same or similar terms as incumbent in-state utilities;
2) siting proceedings should allow or require regulators to account for the regional benefits of new transmission line projects, in addition to benefits to native load customers; and
3) laws providing eminent domain authority should allow projects that provide regional benefits to qualify.

Legal Discussion:

In many states, the "regulatory holdout" problem with transmission line siting is enabled and encouraged by the legal structure of public utility and property law. Entrenched state policies and procedures can present serious obstacles for new entrants in interstate energy markets.

1. Under the utility laws of some states, out-of-state applicants are banned altogether from applying to construct a transmission line. These statutes typically limit applicants to those in-state public utilities that already serve retail customers in that state.[3] State siting authorities — public utility commissions and

[1] Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2571926

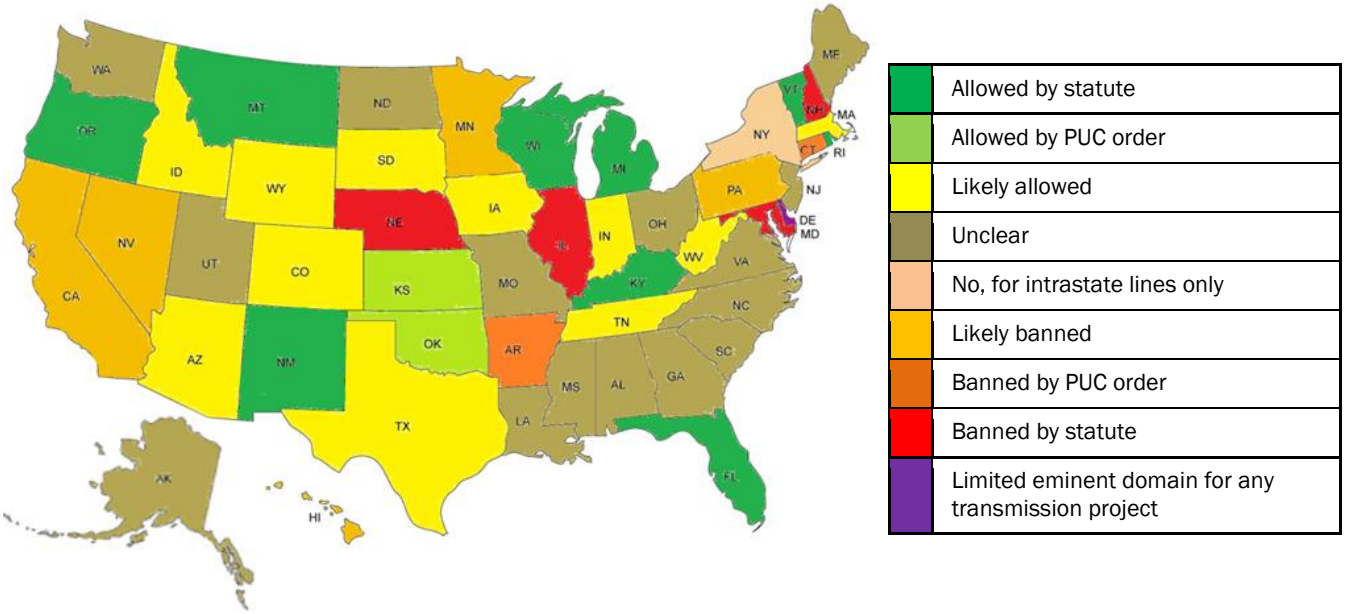
[2] Note that while the dormant Commerce Clause doctrine prohibits regulation of out-of-state transactions, this issue has not yet arisen in the context of interstate transmission line siting.

[3] *See, e.g.,* N.C. GEN. STAT. §§ 62-100, 101 (2014) (allowing only public utilities to construct transmission lines).

other regulatory bodies with jurisdiction over infrastructure siting — sometimes lack the power to even consider project applications brought by developers from outside of the jurisdiction, or they interpret ambiguous statutory authority narrowly.[4] Some states also impose procedural limits on intervention or standing, which prevent out-of-state companies from participating in proceedings where the incumbent utility or a competing in-state developer is proposing to construct a transmission project.

Even if an out-of-state company can apply to obtain siting permission, it may not be able to exercise eminent domain. A handful of states explicitly ban merchant (non-utility) transmission line developers from exercising eminent domain.[5] Most state legal regimes are ambiguous on this point — leaving this discretion to state regulators. For example, in 2012 the Minnesota Public Utility Commission granted siting permission to a merchant transmission developer but noted, without explanation or citation to any authority, that the developer would not have eminent domain powers.[6] Without the threat of eminent domain, a developer maybe be unable to obtain necessary property rights.

Are Merchant Transmission Line Developers Allowed to Exercise Eminent Domain?



2. State regulators may not be allowed to account for the project's out-of-state or regional benefits when they determine whether there is a "need" for the project — resulting in potential discrimination against firms proposing projects that are not devoted primarily to serving retail customers within the jurisdiction. For example, in a strikingly protectionist example of a bias toward in-state benefits, in 2006 Southern California Edison (SCE) proposed to build a 230-mile high voltage transmission line from California to a nuclear power plant, located fifty miles over the Arizona border. California regulators approved the line. However, Arizona regulators rejected the proposal, even though California ratepayers would have paid for the project. The Arizona Commission found that the line was not "necessary to meet the resource adequacy requirements of Arizona utilities."[7] One Arizona regulator bluntly characterized the proposed line as a "230-mile extension cord" for California.

3. Similarly, state property law regimes may skew eminent domain authority in favor of purely in-state projects by in-state actors. States typically limit eminent domain to projects that serve a "public use."

[4] *See, e.g.,* In re Application of Plains & Eastern Clean Line LLC, Order No. 9 (Ark. PUC, Jan. 11, 2011).

[5] *See, e.g.,* 220 ILL. COMP. STAT. § 5/8-509, § 5/8-406.1(a), § 5/3-105(b)(7)): A "qualifying facility" (as defined by PURPA) is not a public utility and thus lacks eminent domain authority. PURPA, 18 C.F.R. § 292.101(b)(i)) – A "qualifying facility" includes transmission lines that "directly and indirectly interconnect [with] electric utilities."

[6] In re Prairie Rose Transmission, LLC, 2012 WL 258025 (Minn. P.U.C., Jan. 13, 2012).

[7] So. Cal. Edison Co., Case No. 130, Decision No. 69638 (Ariz. Corp. Comm'n June 6, 2007), *available at* http://images.edocket.azcc.gov/docketpdf/ 0000073735.pdf.

> While many state property law regimes explicitly state that electric transmission lines are a "public use," others limit such authority to in-state public utilities. Even in states that provide eminent domain authority for electric transmission lines in general, some state courts have limited that authority to projects that provide direct benefits to in-state consumers.[8]

These state laws and practices that inhibit siting and construction of interstate transmission lines are problematic under the dormant Commerce Clause because they discriminate against out-of-state businesses while benefitting in-state interests or burdening interstate commerce. A state can justify discrimination if it can demonstrate a non-protectionist purpose and that it has no less discriminatory means for achieving that purpose. To overcome an argument that its law or practice imposes a burden on interstate commerce, a state can show that the legitimate local benefits outweigh the burden on interstate commerce.

Laws that allow only in-state utilities to construct a transmission line discriminate against out-of-state transmission developers. There is no obvious non-protectionist purpose for this exclusion. The primary beneficiaries are incumbent in-state utilities, which are insulated from out-of-state competition. "Rights of first refusal" favoring incumbent firms, in the form of a non-rebuttable presumption, similarly raise dormant Commerce Clause concerns. States instead should allow out-of-state companies to compete in the transmission market, and use their regulatory process to hold these companies to the same standards as incumbent utilities. Michigan law, for example, requires all applicants to submit and disclose identical information about their proposed projects, and to conduct public meetings.[9] Some states will need to amend their applicable statutes to do this while regulators in other states need only to interpret ambiguous statutes in a manner that treats out-of-state and in-state transmission line applicants evenhandedly.

State siting laws that authorize or require public utility commissions or other regulators to weigh costs and benefits of a line in a manner that leads to rejection of any consideration of the benefits outside of a state's borders are also suspect under the dormant Commerce Clause. Such laws burden interstate commerce and may be discriminatory on their face if they prohibit state regulators from considering out-of-state benefits altogether. A siting statute that allows a regulator discretion to accept or reject a siting application based on its determination of the costs and benefits may not constitute per se discrimination. However, a court could vacate a regulatory decision if regulators apply a facially neutral statute in a discriminatory fashion by excluding out-of-state benefits from consideration.

With regard to eminent domain authority, the dormant Commerce Clause again provides a plausible constraint on how narrowly regulators may assess benefits in their definitions of public use. A restrictive view of "public use" that is limited to in-state benefits is problematic for the same reasons that public utility regulators' narrow "need" assessments may run afoul of the dormant Commerce Clause. Where state laws are ambiguous on the scope of public use, regulators are typically allowed to adopt — and best practices would favor — a broad, regional approach.

The dormant Commerce Clause does not prevent a state from addressing valid land use concerns and should not be seen as a mandate that all transmission projects are entitled to approval and eminent domain authority, regardless of their merit. Rather, the dormant Commerce Clause requires states to define "public use" in a non-discriminatory way that allows projects proposed by out-of-state actors or that provide regional benefits to qualify for the privilege. Following the Supreme Court's decision in *Kelo v. City of New London* in 2005,[10] more than half of states revised their eminent domain laws to more narrowly define what constitutes a "public use" to limit general eminent domain authority. States should ensure that these laws expressly recognize that any

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[8] Square Butte Electric Cooperative v. Hilken, 244 N.W.2d 519, 525 (N.D. 1976); *see also* Clark v. Gulf Power Co., 198 So.2d 368 (Fla. 1st D.C. App. 1967) (holding that eminent domain power exists "for the use and benefit of the people within the state").

[9] MICH. COMP. LAWS ANN. § 460.564–71.

[10] The Court held that a city's decision to take private property by eminent domain in connection with a private redevelopment project was a "public use" under the Takings Clause of the Fifth Amendment.

facility that is required to transport energy as a common carrier or utility in interstate commerce qualifies as a public use.

Conclusion

Many siting regimes are steeped in longstanding traditions of local land use regulation or in siting statutes that predate the contemporary changes that have transformed energy industries. Such regimes allow regulators to hide behind the complacency of the status quo, sometimes benefitting in-state monopolists at the expense of out-of-state firms seeking to compete in the market for interstate energy infrastructure. These laws hinder the development of interstate markets and are problematic under the dormant Commerce Clause. States should evaluate their existing laws and regulatory practices to make sure they are allowing for interstate competition in the transmission market.

Eminent Domain Statutory Supplement[11]

Examples of state laws that grant eminent domain authority to merchant transmission developers:

- Michigan (MICH. COMP. LAWS ANN. § 486.255) ". . . an independent transmission company or an affiliated transmission company shall have the power to condemn property that is necessary to transmit electric energy for public use . . ."
- New Mexico (N.M. STAT. ANN. § 62-16A-4 (B)(8)) The New Mexico Renewable Energy Transmission Authority may, "pursuant to the provisions of the Eminent Domain Code, exercise the power of eminent domain for acquiring property or rights of way for public use if needed for projects if such action does not involve taking utility property or does not materially diminish electric service reliability of the transmission system in New Mexico, as determined by the public regulation commission."

Examples of state laws that support eminent domain for interstate transmission lines:

- Kansas (KAN. STAT. ANN. § 74-99d01, § 74-99d07(a)(15-16), § 74-99d08(b) (2012)) (creating the Kansas Electric Transmission Authority to "further ensure planning and reliable operation of the integrated electrical transmission system," providing the Authority with eminent domain powers, and focusing on economic development and regional reliability benefits of transmission projects).
- Idaho (Idaho Energy Resources Authority Act, IDAHO CODE ANN. § 67-8902, § 67-8908(g) (2012)) (creating the Idaho Energy Resources Authority, providing the Authority with eminent domain powers, and focusing on reliability improvements offered by interstate lines).

Examples of state laws that encourage interstate transmission development

- New Mexico (Renewable Energy Transmission Authority Act, N.M. STAT. ANN. § 62-16A-4 (2012)) "The authority may . . . through participation in appropriate regional transmission forums, coordinate, investigate, plan, prioritize and negotiate with entities within and outside the state for the establishment of interstate transmission corridors." . . . and "[t]he authority may . . . pursuant to the provisions of the Eminent Domain Code, exercise the power of eminent domain for acquiring property or rights of way for public use if needed for projects . . ."
- Wyoming WYO. STAT. ANN. §§ 37-5-303(a), 37-5-304(a)(iv-v) (2012) (creating the Wyoming Infrastructure Authority whose purpose is to "diversify and expand the Wyoming Economy through improvements in the state's electricity transmission infrastructure and to facilitate the consumption of Wyoming energy," and which can plan, own, develop, and maintain infrastructure within and outside of Wyoming to accomplish its purpose and acquire property by condemnation for those purposes).

[11] For a more detailed discussion of the law in all 50 states, see Alexandra B. Klass, Takings and Transmission, 91 N.C. L. REV. 1079 (2013), available at: http://www.nclawreview.org/documents/91/4/klass.pdf.