

## **Cooperative Renewable Energy Policies to Avoid Trade Related Disputes and Litigation<sup>1</sup>**

### **INTRODUCTION**

Over the next three decades, world energy consumption is projected to increase by 56 percent. (EIA, 2013). Fossil fuels are expected to continue to supply almost 80 percent of world energy through 2040, but faced with rising energy prices and supply uncertainties, as well as mounting concerns over the social effects of climate change, many governments on the state and national level have begun to diversify energy options and seek cleaner alternatives to traditional fossil fuel combustion. Due to the lack of multi-national leadership for a global climate change solution, lawmakers have begun to facilitate the development of sources of renewable energy including onshore and offshore wind energy, as well as solar and geothermal power, fuel cells, and biomass.

The need for, and awareness of, clean energy coincided with a global economic recession, and policy makers have responded with “green” energy laws that promote the development of these renewable energy resources, as well as create localized economic benefits. (EIA, 2013). Many states, regions, and countries have set aggressive carbon emissions goals and renewable portfolio standards, along with local content provisions that encourage or mandate localized renewable energy production and facility development.

New renewable energy facilities need to be built from the ground-up in this fledgling industry, and development of renewable energy provides clean carbon-free power and typically stimulates the local economy through job creation. However, there is an inherent tension presented with renewable energy technology development: these technologies are less damaging to the environment than traditional fossil fuels, but the costs to develop and deliver this clean technology will initially be more expensive than utilizing the existing fossil fuel infrastructure and industry know-how. Arguably, while the ratepayer will ultimately recognize cost savings through the development of renewable energy technologies (such as reductions in human mortality and morbidity from the emission of pollutants such as particulate matter and NO<sub>x</sub>, avoided greenhouse gas emissions, the value of fuel saved, and greater energy independence), in

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order to understand the true costs of various forms of electricity generation technology, it would be necessary to remove all market distortions and internalize the external costs of energy generation. (Sheridan, 2013). The general public does not recognize the value of these external costs, but when the initial capital costs associated with renewable energy development are passed onto the ratepayer, the dollar value is plain to see on a utility bill.

While increased energy bills are not popular with the general public, economic growth is favored and easily relatable, and many lawmakers, who are interested in maintaining their office and keeping their constituents happy, have begun to include local incentives that promote in-state generation of renewable energy in order to spur local job growth. However, the local content provisions of these laws may include elements of economic protectionism, which may violate the dormant commerce clause of the United States Constitution, and may also run afoul of international trade law regimes, such as the World Trade Organization.

Economic protectionism usually comes in the form of import controls. Trade disputes occur when policies are enacted into laws that create an uneven playing field by controlling the flow of imports in a manner that one or more stakeholder believes to be unfair. This may occur when a state drafts a law that contains a 'home-grown' requirement that requires that a certain percentage of energy, for example, be produced within the jurisdictional boundaries of the state. Such policies are enacted and justified for economic or strategic reasons, and the goal of protectionism is typically to give greater advantage and favor domestic/local industry to the detriment of foreign industry. The result of such action may have effects on supply and demand and free market forces.

In the U.S. and internationally, several laws have recently come under attack for their economic protectionist policies. Interestingly, these laws contain provisions that are facially indefensible, yet nonetheless, lawmakers continue to draft exclusionary laws in order to achieve renewable energy goals, such as renewable portfolio standards ("RPS") standards. In recent years, these protectionist laws have led to litigation on the state and international level, and the ramifications of these actions have had, and may continue to have, significantly negative impacts of renewable energy development.

This paper will examine two trade-related renewable energy disputes concerning economically protectionist policies: the international dispute between Japan and Canada in the World Trade Organization ("WTO"); and a constitutional lawsuit by a private company suing

over the state of Massachusetts' Green Communities Act. While these cases are unique in the renewable energy context, in that the WTO case addressed feed-in-tariffs and renewable energy subsidies, and the litigation in Massachusetts is the only dormant Commerce Clause challenge to a renewable portfolio standard that has been resolved to date,<sup>2</sup> the focus of this paper will be to discuss the elements of economic protectionism in each of the laws, highlight the significance of the litigation, and discuss lessons learned from each of these case studies. Using the two cases as a cautionary tale, this paper will explore the various policies that may be adopted to support renewable energy development without implicating litigable economically protectionist measures. The paper will present options for policy makers who are trying to avoid litigation over such measures, and will present lawmakers with collaborative options to consider when creating policies to promote renewable energy development.

### **Case Study I: The World Trade Organization Dispute Between Japan and Canada**

In September of 2010, Japan initiated a trade dispute against Canada in the WTO related to Ontario's local content renewable energy requirement. This dispute was the first of its kind in the WTO that directly addressed a country's feed-in-tariffs and examined a renewable energy subsidy.

#### Canada

In 2008, the Canadian economy was deeply affected by the global recession. Canada faced its second-largest overall decline in real output since the Great Depression, and job losses were staggering. In the province of Ontario, the effects of a weak global environment accelerated in 2009, and gross domestic product (GDP) fell 3.1%. Most of the job losses occurred in manufacturing, followed by wholesale activity and construction to a lesser extent.

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<sup>2</sup> Notably, in a recent ruling from June, 2013, Judge Richard Posner, a member of the U.S. Court of Appeals for the 7th Circuit, voiced his concern over a Michigan statute that "forbids Michigan utilities to count renewable energy generated outside the state toward satisfying the [RPS] requirement . . ." *Illinois Commerce Com'n v. Federal Energy Regulatory Com'n*, 721 F.3d 764,775-76 (7th Cir. 2013). Judge Posner stated that this component of the RPS program "trips over an insurmountable constitutional objection [and] Michigan cannot, without violating the commerce clause of Article I of the Constitution, discriminate against out-of-state renewable energy." *Id.* While Judge Posner's language about the Commerce Clause is considered non-binding dictum because the constitutionality of Michigan's RPS was not part of the dispute, his position on Michigan's RPS is nevertheless problematic for a number of states that have RPSs with similar local content requirements.

Overall, 17 of the 21 major manufacturing industry groups posted declines for the fiscal year. (Foreign Affairs, 2010).

Ontario, which is Canada's most populous province, launched an incentive program for renewable energy producers in October of 2009 that aimed to create jobs and eliminate coal-fired power generators. In order to mitigate the effects of climate change, Ontario adopted a comprehensive and aggressive energy development plan to encourage local development of renewable energy. Their program, known as the Green Energy Act ("GEA"), guaranteed long-term pricing to solar and wind producers who manufacture a minimum percentage of locally produced components.

The Act sought to foster "growth of renewable energy projects, which use cleaner sources of energy" by "removing barriers to and promoting opportunities for renewable energy projects and to promoting a green economy." (Bill 150, 2009). The Act focused on: 1) bringing more renewables to the province; and 2) creation of more energy efficiency measures to help conserve energy.

The Act guaranteed long-term pricing to solar and wind producers who manufacture a minimum percentage of locally produced components, and the central plank of the green energy program was a domestic content, or "made-in-Ontario" requirement. Schedule (6)(1)(h)(vi) of the Act required that the Ministry of Energy "stimulate the planning and increase the development of infrastructure in Ontario." (Bill 150, 2009). The Act further demanded that up to 60% of all green energy project inputs be manufactured in the province. Ontario's incentives, also known as feed-in tariffs, offered above-market prices on a technology-by-technology basis to producers of energy from clean, renewable sources like the sun and wind. By increasing local manufacturing investment, the GEA sought to spur job creation.

Initially, the GEA appeared to succeed in several of its goals. In just a few short months, the program attracted several large foreign wind power companies to the province. In January, 2010, South Korea's Samsung C&T unveiled a \$6.8 billion investment in Ontario. The Ontario provincial government offered to support the company through preferential grid access, subsidies and land. (Shah, 2010). Samsung pledged to support local infrastructure development in Ontario for the renewable energy industry by constructing production facilities to provide key components like turbine blades, wind towers, solar modules and inverters. Samsung also encouraged component suppliers, such as Germany-based Siemens, to build manufacturing

facilities in the area. In total, the project was expected to generate more than 16,000 green energy jobs within Ontario. (Samsung, 2010).

### Japan:

In recent years, as part of strategic economic development, Japan has expressed keen interest in the international green energy/clean technology market and has begun to establish itself as “the homeland of modern green technology,” with conglomerates like Sharp, Mitsubishi, Kyocera and others coming forward as industry leaders in clean technology. (JETRO, 2010). In early 2010, Peter M. Fannon, Vice President of Corporate & Government Affairs at Panasonic Corp. of North America, stated that Panasonic’s primary corporate goal is “to be the #1 green innovations company in the electronics industry.” (CleanTech, 2008). Many current green technologies have been spearheaded by Japanese companies, and Japanese powerhouses, such as Panasonic, have begun to develop clean technology.

In 2008, Japan’s prime minister announced plans to create a \$10 billion fund to help emerging countries reduce emissions. The five-year fund, called the Cool Earth Partnership, was financed by government and business, and set aside \$8 billion for climate change mitigation, and up to \$2 billion for grants, aid and technical assistance for countries switching to renewable energy. (CleanTech, 2008). The plans included a \$30 billion investment in research and development in the environment and energy sectors and developing countries over five years.

With the Japanese government investing in development funds, and companies aggressively pursuing technological advantages, Japan’s clean technology sector was gearing up to build brand loyalty while also seeking to ensure long-term maintenance contracts with development of renewable energy facilities. By developing and providing clean technology components for installation in developing countries, Japanese companies had been steadily emerging as world leaders in clean energy technology.

However, there was intense competition for lucrative renewable energy contracts, and as the global market for renewable technology grew, Japanese industries began to dramatically lose their market share in several areas to foreign companies, such as Samsung. (Yanase, 2010). As an example of lost opportunities to secure large contracts, in early 2010, the Ontario government awarded a multibillion-dollar deal to a consortium led by Korea-based Samsung Group. (Samsung, 2010).

## The Dispute in the WTO

As a member-based international trade organization, the WTO provides a forum for member states to maintain an open trade market, and allows for binding dispute resolution if grievances arise between member states. The main principles of the WTO Trading System involve trade without discrimination (including most-favored-nation (“MFN”) status, where countries cannot discriminate between their trading partners, national treatment (which involves treating foreigners and locals equally)), as well as freer trade, which is to be achieved gradually, through negotiation. (WTO Principles, 2012). The remaining tenets concern promotion of fair competition, and encouraging development and economic reform.

In September of 2010, Japan formally aired their grievances in the WTO over the GEA, and filed a complaint, or “Request for Consultation” with the WTO against Canada. In their filing, Japan alleged that Ontario’s local content renewable energy requirement was a subsidy program that contravened the WTO rules that ban unfair treatment of import products. The dispute centered on guaranteed long-term pricing for solar and wind generators made with a certain percentage of locally produced components, and Japan argued that Ontario’s pricing guarantees in the wind and solar sectors constituted subsidies that violated Canada’s obligations under international trade law. (WTO DS412, 2010).

In December of 2012, the WTO issued its initial ruling in the dispute, largely finding that Canada’s measures violated its obligations under international trade law. This ruling was upheld in May of 2013. As discussed in further detail below, in light of the WTO’s final ruling, Ontario was forced to reassess its laws in order for Canada to stay in compliance with their commitments under the WTO.

## Japan’s Request for Consultation

In response to Ontario’s GEA, on September 13, 2010, Japan filed a complaint, or ‘Request for Consultation’ with the WTO against Canada. The Japanese request for consultations was the first step in a WTO dispute. In their filing, Japan alleged that the Ontario subsidy program contravened the WTO rules that ban unfair treatment of import products. The Japanese mission to the WTO said the dispute centered on guaranteed long-term pricing for solar and wind generators made with a certain percentage of locally produced components. Japan

alleged that Ontario's wind and solar pricing guarantees constituted subsidies that violated Canada's obligations under international trade law. (WTO Dispute, 2010).

On September 24, 2010, the United States requested to join the consultations and on September 27, 2010, the European Union also requested to join the consultations. The 1994 General Agreement on Tariffs and Trade (GATT 1994), which the WTO administers, includes provisions permit third parties, including other Member countries and the WTO Secretariat, to mediate in a dispute and take part in the consultations. (WTO Legal, 2010). Third party Members with a 'substantial trade interest' in a dispute may also engage in the consultation process, subject to the agreement of the respondent.

Canada accepted the requests of the E.U. and the U.S. to join the consultations, and in July 2011, the Dispute Settlement Board accepted Japan's request to establish a panel. The WTO Dispute Panel is a three to five member panel that investigates the evidence in the context of the relevant provisions of the WTO agreements cited, and then makes recommendations or rulings to the Dispute Settlement Board ("DSB") with regard to the relevant WTO agreements. The Panel can then take up to twelve to fifteen months to make a Final Panel Report. (Zekos, 2009). In addition to Japan, several other WTO members<sup>3</sup> with a 'substantial trade interest' in the dispute also reserved their third party-rights to engage in the consultation process. (WTO DS412, 2010).

### Japan's Allegations

Japan alleged that the Canadian GEA created a subsidy that was prohibited under the Subsidies and Countervailing Measures Agreement ("SCM Agreement"), located in Articles 3.1(b) and 3.2. The SCM Agreement specifies under which circumstances Members can provide subsidies, and the use of countervailing measures to offset injury caused by subsidized imports. (WTO SCM, 2013). The SCM Agreement may be enforced through invocation of the WTO dispute settlement mechanism.

In pertinent part, Sections 3.1(b) and 3.2 state that "subsidies . . . shall be prohibited . . . [if they are] contingent . . . upon the use of domestic over imported goods" and that each "Member shall neither grant nor maintain [such] subsidies . . ." The Japanese claims alleged that

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<sup>3</sup> The third parties that expressed an 'substantial trade interest' were: Australia; Brazil; China; El Salvador; the E.U.; Honduras; India; Saudi Arabia; South Korea; Mexico; Norway; Chinese Taipei; and the United States.

the subsidy, which would only be awarded if the energy was produced at an Ontario-based generation facility, conferred a benefit for Ontario and that the law made such use preferable over equipment imported from other countries, such as Japan. (WTO DS412, 2010).

Japan next claimed that the GEA violated Article 2:1 of Trade-Related Investment Measures (“TRIMs”). TRIMs restrict Members from engaging in practices that have the effect of preferring domestic firms. The TRIMs Agreement, which is another component of the WTO that all Members agreed upon, defines the domestic regulations that a country can apply to foreign investors. Japan alleged that the local content requirement component of the GEA was inconsistent with the TRIMs, and that the law favored Canadian firms by providing subsidies contingent upon the use of domestic over imported goods. In their Request for Consultations, Japan also alleged that the GEA accorded less favorable treatment to imported equipment than to products originating in Ontario, and that these trade-related investment measures were inconsistent with the provisions of Articles III:4 and III:5 of the GATT 1994.

In pertinent part, Article III:4 states:

the products of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

(WTO DS412, 2010). Likewise, Article III:5 of the GATT states:

No contracting party shall establish or maintain any internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources. (WTO DS412, 2010).

Japan alleged that the GEA accorded less favorable treatment to imported equipment than to products originating in Ontario. The allegation further stated that Ontario’s internal quantitative regulations appeared to require that equipment for renewable energy generation



facilities be supplied from Ontario sources. Japan alleged that these ‘specified amount’ provisions were contrary to the principles of Article III of the GATT 1994. (WTO DS412, 2010).

In defense of their programs, Canada argued that the FIT program was a form of government procurement designed to ensure the affordable generation of clean energy in Ontario, and that the GATT national treatment requirements and the TRIMS Agreement provisions should not apply to the program. (ITSCD, 2012). The Canadian delegation further argued that the program qualified as government procurement that would also be exempt from the WTO subsidies agreement provided that it did not confer a benefit.

### Resolution of the WTO Dispute

On December 19, 2012, the Panel ruled on Japan’s complaint against Canada, and found that Ontario’s feed-in-tariff program violated Canada’s obligations under the WTO. Specifically, the WTO panel upheld Japan’s claims under Article 2:1 of the TRIMs Agreement and Article III:4 of the GATT 1994, finding that the GEA included trade measures which included mandatory requirements under domestic law and required the purchase or use of products of domestic origin. (WTO DS412, 2012). The WTO affirmed Japan’s accusations that Ontario’s renewable energy feed-in-tariffs, which required 60% of equipment to come from locally made sources, breached the WTO’s non-discrimination principle enshrined in the GATT and the TRIMS.

However, the WTO panel rejected the claim that the feed-in-tariff program constituted an illegal subsidy. While the three-member panel issued a divided ruling in response to Japan’s claim under Articles 3.1(b) and 3.2 of the SCM Agreement, the panel majority found that Japan failed to establish the existence of a subsidy and that there was an insufficient benchmark to determine if the GEA conferred a “benefit” to Ontario electricity producers. (WTO DS412, 2010). The sole dissenter on the WTO panel found that Japan had succeeded in demonstrating that the challenged measure conferred a “benefit” to Ontario in contravention of Article 1.1(b) of the SCM Agreement.

The DSB then reviewed the Final Panel Report and its recommendations, and adopted the findings. Upon adopting the Panel’s report, its recommendations became binding on the parties to the dispute. (WTO Legal, 2010).

In February, 2013, Canada filed a timely appeal to the Appellate Body of the WTO, and Japan and followed suit with a cross-appeal. In May 2013, the Appellate Body circulated its report to the Members, and affirmed most of the December ruling. The Appellate Body essentially dismissed Canada's appeal and confirmed that Ontario's rules are discriminatory and in breach of the WTO Agreement.

Under WTO rules, the Appellate Body report was adopted by the WTO Dispute Settlement Body within 30 days, and Canada was tasked with presenting its plan for implementing the ruling within the following month. For its part, the Canadian federal government said it would work with the province to address the ruling's implications. "As this is the first time Canada has received a WTO panel ruling arising solely from provincial policy or legislation, we will work with the Ontario government in order to respond to the decision," said Caitlin Workman, spokesperson for the Department of Foreign Affairs and International Trade. (CBC News, 2010).

In response to the WTO ruling that the GEA contravened international trade law, Ontario made several changes to the GEA. Ontario slashed the subsidies that it had previously offered to build turbine towers and blades, and in May 2013, Ontario dropped its feed-in tariff program for large-scale renewable energy projects and made changes to its local content regulations for wind farms. (NAWP, 2013). Further, while the deal between Ontario and Samsung has been retained, it was revised in number of ways, most notably the contract was reduced from 2.5GW to 1.369GW and Ontario will now only buy C\$6 billion worth of electricity from Samsung, a reduction of C\$3.7 billion. (WPM, 2013). Samsung also reduced its original investment commitment in new manufacturing plants and renewable energy projects in the province from C\$7 billion to C\$5 billion.

### **Case Study II: The Dormant Commerce Clause Litigation over the Massachusetts Green Communities Act**

As with Ontario, several states within the United States have enacted policies that promote in-state generation of renewable energy in an attempt to mitigate the effects of climate change, promote renewable energy sources, and spur economic development. When developing various green energy policies, state policy makers have included various financial incentives to promote development of green energy, including tax incentives, grant programs, green building

incentives, and rebate programs. Renewable portfolio standards (“RPS”), which mandate that a certain percentage of energy production come from renewable sources, such as wind, solar, geothermal or biomass, have grown in popularity, as state law makers seek to add renewable energy to the electricity mix.

In order to advance the mandates of the state RPSs, several state legislators have included incentives that favor in-state generation of renewable energy. These incentives typically encourage local renewable energy production by offering financial assistance for localized facility development. Arguably, these local content provisions of the green energy laws are developed so that when state constituents are asked to pay potentially higher electricity bills, state legislators can point to the more appreciable tangible benefits as an offset, such as local jobs.

While such laws benefit the home state, these ‘home-grown green energy’ efforts tend to have economic consequences for the free market and may run afoul of the dormant commerce clause of the U.S. Constitution. Economically protectionist features of the state laws may violate the constitution if they exclude and/or disfavor out-of-state goods (energy) in favor of in-state goods. Such economically protectionist laws may prohibit free trade among the states by placing state welfare over and above the welfare of the many states. If they do, these restrictions on trade and interstate commerce conflict with the dormant Commerce Clause of the U.S. Constitution, and offend the supremacy of federal laws.

The discussion below reviews the dormant Commerce Clause in the context of the litigation over the Massachusetts Green Communities Act, and encourages policy makers to find a cooperative solution to encourage the development of renewable energy without trade restrictions and the attendant market distortions.

### The Dormant Commerce Clause

The U.S. Constitution provides Congress with certain enumerated powers, and Article 1 specifically provides that Congress has authority to “regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.” Thus, Congressional commerce power (or the “Commerce Clause”) is limited to interstate, foreign and tribal commerce. Pursuant to the Tenth Amendment, the “powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the

people.” The term “dormant Commerce Clause” was adopted through a body of case law in which the Supreme Court decided that this clause also inferentially involved restrictions on state power that are inherent to the Commerce Clause of the Constitution. Individual states therefore have internal ‘police powers,’ such as the ability to regulate for the health, safety, welfare, and morals of that state. The powers of intrastate commerce, as opposed to Congressional power over interstate commerce, are therefore reserved for the individual states to regulate and legislate independently.

However, state laws cannot burden interstate commerce, and individual/state actions cannot have a substantial cumulative effect on interstate commerce. To allow a state to do so would take away from the supremacy of federal law and would create tensions among the states of the union. Therefore, the dormant Commerce Clause dictates that states are prohibited from passing legislation that improperly burdens or discriminates against interstate commerce. When the dormant Commerce Clause is invoked, and parties sue over the constitutionality of a state law, state laws that are facially discriminatory (laws that explicitly favor in-state over out-of-state goods) are considered *per se* invalid and are subject to strict judicial scrutiny. (Philadelphia, 1978).

State laws also cannot disguise an economically protectionist law as a legitimate regulation, and state goals, such as an RPS, cannot be “accomplished by discriminating against articles of commerce coming from outside the State unless there is some reason, apart from their origin, to treat them differently.” (Philadelphia, 1978). Moreover, “a State may not insulate part of its market from out-of-state competition” even if other parts are left open, and a state law that causes “local goods to constitute a larger share, and goods with an out-of-state source to constitute a smaller share, of the total sales in the market, is unconstitutional.” (Cloverland, 2006). The exclusion of out-of-state manufacturers has the effect of providing ongoing advantages to in-state firms, and subsidies to in-state firms also thwart the market economy by skewing standard market fluctuations.

#### The Massachusetts Green Communities Act

The Massachusetts Green Communities Act (“GCA”) was signed into law on July 8, 2008, by Governor Deval Patrick. The GCA was a comprehensive energy reform bill intended to reduce electric bills, promote the development of renewable energy and stimulate the clean

energy industry in Massachusetts. The law placed Massachusetts at the national forefront of climate change reform, with a RPS requirement of 25% of energy consumption to be from renewable resources by 2030. (Mass EEA, 2013; MDER, 2010).

The initial Massachusetts RPS, passed and signed into law in the Massachusetts General Law Chapter 25a, Section 11F, stated that “(g) each retail supplier shall provide a portion of the required minimum percentage of kilowatt-hours sales from new on-site renewable energy generating sources located in the commonwealth...

(h) [alternately the] retail supplier [can] discharge its obligations under subsection (g) by making an alternative compliance payment [ACP] in an amount established by the department; provided...that the department shall set ACP rates at levels that shall stimulate the development of new on-site renewable energy generating sources.

The GCA updated the Massachusetts RPS, and the RPS was broken into two different classes, with the annual RPS obligation set to increase by 1% each year. (Mass EEA, 2013; MDER, 2010).

Specifically, two sections of the GCA included incentives for in-state generation of renewable energy. Section 32 of the GCA provided for a solar carve-out, and stated that out-of-state solar producers would not qualify for solar renewable energy credit (“SREC”) charge, and that retail suppliers would be charged an ACP if they did not get their energy from ‘ineligible’ out-of-state producers. Section 83 of the law required utility companies to enter into long term (10-15 year) contracts with renewable energy developers to help developers of clean energy technology obtain financing to build their projects. This section specified that these companies must be located in Massachusetts. Furthermore, the agreements target Massachusetts-based projects between 2009-2014, noting that utility companies: “shall...solicit proposals from renewable energy developers and, provided reasonable proposals have been received, enter into cost-effective long-term contracts to facilitate the financing of renewable energy generation within the jurisdictional boundaries of the commonwealth, including state waters, or in adjacent federal waters.”

In April 2010, the GCA came under attack by TransCanada Corporation (“TransCanada”), which operates pipelines and owns interests in power plants in Canada, the U.S. and Mexico. (TransCanada, 2010). TransCanada had recently invested in the Kibby Wind Farm, a 132MW land-based wind power facility located in Eustis, Maine. TransCanada, which

had been contemplating a potential 45MW expansion for the Kibby Wind Farm, filed a lawsuit in U.S. District Court for the District of Massachusetts (Central Division) suing a number of high-level Massachusetts officials over provisions in the GCA. The action named as defendants Ian A. Bowles, Secretary of Massachusetts Executive Office of Energy and Environmental Affairs, Philip Giudice, Commissioner of Massachusetts Department of Energy Resources (DOER), Paul J. Hibbard, Chairman of Department of Public Utilities (DPU), Tim Woolf, Commissioner of DPU, and Jolette A. Westbrook, Commissioner of DPU.

TransCanada alleged that Massachusetts laws violated the dormant Commerce Clause by preventing power from their Maine-based Kibby Wind Plant to be sold in Massachusetts. It alleged that the Massachusetts law explicitly discriminated in favor of in-state economic interests through the creation of discriminatory qualification requirements for energy providers, a tariff-subsidy available only to support in-state companies, and use of discriminatory renewable energy multipliers that further encourage electricity generation by in-state energy providers over their out-of-state competitors. (TransCanada, 2010). TransCanada argued that the law was motivated by economic protectionism and had the purpose and effect of shielding politically-favored, in-state companies from competition and forcing state ratepayers to subsidize their development. Essentially, the TransCanada lawsuit claimed that the GCA burdened interstate commerce and discriminated against out-of-state economic interests by denying them equal competitive footing with in-state companies.

TransCanada challenged the law because it had existing contracts and would have to pay an ACP penalty since its generation was not in-state and in that regard, raised two concerns with two specific programs: 1) the solar carve out; and 2) the broader RPS program. On the issue of the solar carve out, TransCanada argued that the law, which excluded out-of-state solar facilities from SREC eligibility, discriminated against out-of-state electricity providers. (TransCanada, 2010). On the second issue, the broader RPS program, which required utilities and energy suppliers to negotiate contracts with in-state projects, TransCanada alleged that Section 83 of the GCA prevented it from selling wind electricity from Maine into Massachusetts and that the law discriminated against out-of-state renewable energy projects in violation of the U.S. Constitution. (TransCanada, 2010).

The constitutional merits of the solar carve out were never fully litigated, as the parties quickly settled this component of the lawsuit. On May 29, 2010, TransCanada agreed to drop its

claims against the state's solar program after Massachusetts agreed to 'grandfather' contracts, including TransCanada's contract, that were signed prior to 2010. 'Grandfathered' suppliers would not have to pay the higher ACP fees for being out-of-compliance with the state's renewable energy goals.

The litigation over the RPS program was slightly more protracted, with the parties engaging in motion practice for several months. However, this dispute also never reached the merits in the courthouse, because the Massachusetts Department of Public Utilities ("DPU") issued an emergency ruling eliminating the in-state requirement from the regulation that mandates electric utilities buy their renewable energy from projects installed in Massachusetts or off-shore wind in the Cape Cod area. The emergency rule came just nine days after TransCanada filed a notice of dismissal "with prejudice" to drop its lawsuit against the three named individual commissioners of the DPU. The Boston Herald observed that the state legislature apparently suspected that the provision was unconstitutional when it enacted the GCA because the act specifically allowed the DPU to strike the provision in the event of legal challenge. (McCarter, 2010).

Although the TransCanada dispute did not yield a court decision on the constitutionality of in-state renewable energy procurement requirements, Massachusetts' willingness to settle and back-peddle from the protectionist elements of the law demonstrates the vulnerability of the in-state contracting requirements and in-state carve-outs of the RPS. Without a court decision on the merits of either of the issues in the TransCanada case, the door is open for other stakeholders to sue over the components of the law that favor in-state generation.

The question remains how far a state can go in promoting in-state installations of renewable energy projects without running afoul of the dormant commerce clause of the U.S. Constitution. The failure to fully litigate this issue begs the question of whether a state can survive a constitutional attack if it mandates in-state renewable installations in exchange for in-state qualifying renewable energy certificates.

### **DISCUSSION: Creating Legally Defensible Solutions**

These cases are unique in that the WTO case is the first of its kind to address feed-in-tariffs as a renewable subsidy, and the litigation in Massachusetts is the only dormant Commerce Clause challenge to an RPS that has been resolved to date. When examined together, these two

cases demonstrate that there are legal implications when policymakers create laws that have economically protectionist effects and operate to the detriment of free trade with interested states. These trade disputes stemmed from laws that created an uneven playing field by exerting control over the flow of imports in a manner that litigants believed to be unfair. Yet, the policy makers in Ontario and Massachusetts justified the enactment of these vulnerable policies for economic and political reasons, i.e., to give local industry a greater advantage to the detriment of outsiders, and to give economic benefits to their constituent base, such as job creation, improvements in air quality, increased tourism, and the image of the state as a ‘first adopter,’ including branding and marketing value for the region. When being asked to subsidize the costs of a new technology, such as offshore wind, ratepayers want to ultimately reap the economic benefits, and political backlash may occur if ratepayers are asked to effectively subsidize the costs of the new technology without relatable and tangible benefits that stem from renewable energy policies.

In both cases, lawmakers were forced to reverse course and change policies and laws in response to litigation. Such weaknesses in the law do not instill investor confidence and may discourage companies from making capital investments when there is a threat that subsidies may be withdrawn if laws are rewritten or overruled. The specter of litigation also has a chilling effect on investment, and industry may be slowed down when litigation has been drawn out for years.<sup>4</sup> In addition to the legality of these laws, and the attendant threats of litigation, the debate surrounding these laws may disrupt positive momentum and cause waning public support of renewable energy development.

These cases should serve as a deterrent to policy makers that are attempting to draft laws with protectionist underpinnings. In order to avoid litigation, law and policy makers must find a balance between drafting legally defensible laws, developing economically reasonable projects, achieving state renewable energy goals, and working collaboratively to create solutions that do not create direct conflicts with the dormant commerce clause or WTO tenets.

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<sup>4</sup> The protracted litigation surrounding the Massachusetts Cape Wind proposal provides a good example of how litigation has affected offshore wind energy development. See Williams, W., & Whitcomb, R. (2007). *Cape Wind: Money, Celebrity, Energy, Class, Politics, and the Battle for Our Energy Future*. New York: Public Affairs.



## Drafting Legally Defensible Policies

States may have legitimate environmental objectives for in-state power generation, as new in-state renewable power plants may improve its air quality, displace fossil-fuel based generation, and may also avoid costs associated with new transmission lines and congestion fees. (Lehfeldt, et al., 2010). Arguably, in-state generation will confer benefits and can serve legitimate local purposes that cannot be adequately achieved by reasonable nondiscriminatory alternatives. So while there may be room for states to favor local development, lawmakers may nonetheless want to draft laws that still encourage a degree of local production but that are less obviously protectionist in order to avoid problems with the Commerce Clause and running afoul of WTO laws. Lawmakers can consider whether a location-based requirement can be recast in more neutral terms so that it stands a better chance of surviving scrutiny under the WTO or the Commerce Clause.

Some states such as Colorado and Missouri apply multipliers to renewable energy certificates produced from in-state resources. (DSIRE CO, 2014; DSIRE MO, 2014). New Jersey laws include both out-of-state and in-state manufacturers as eligible participants, and “Class II” renewable energy is defined as electricity generated by facilities located in NJ or outside of NJ if the facility is located in a state with retail electric competition and the facility is approved by the Department of Environmental Protection. (DSIRE NJ, 2014). Delaware granted a 150% credit toward RPS compliance for energy generated by wind turbines sited in Delaware on or before December 31, 2012, and grants a 110% credit for solar or wind installations sited in Delaware for which at least 50% of the equipment or components are manufactured in Delaware or installed with a minimum 75% state workforce. (DSIRE DE, 2014).

Moreover, policies that are drafted to confer ‘net benefits’ to local citizens may be less vulnerable to scrutiny and litigation. Net benefits are defined differently based on the various stakeholders’ economic values, but generally, in order to justify expenditures and increased energy costs for ratepayers, it is important to establish that a project is economically reasonable and creates sufficient benefits.

Although no offshore wind facilities have yet been built in the U.S., several states have sought to incentivize offshore wind in a way that “fairly balances the risks and rewards of the project between ratepayers and shareholders.” (Rate Counsel, 2013). For example, through

policies such as New Jersey Governor Chris Christie's 2011 Energy Master Plan ("EMP") and laws such as the Offshore Wind Economic Development Act, ("OWEDA"), the state of New Jersey has expressed its support for offshore wind, citing the fact that it "has no carbon output, and has the potential to develop a manufacturing and support industry within the State, thereby creating direct, indirect, and induced economic benefits for many years to come." (NJ EMP, 2011). Through the implementation of the EMP and OWEDA, New Jersey ensures that renewable energy projects are developed with appropriate consideration of the impact on ratepayers and the need to attract investment to the state. Through renewable energy development, the state has a statutory requirement to provide net benefits to the state's ratepayers, and developers must guarantee direct jobs and direct expenditures in New Jersey substantiate such figures with vendor quotes and provide documentation of economic benefits. (Rate Counsel, 2013).

#### Policy Alternatives for Cooperative Action

In order to encourage renewable energy development, lawmakers should move away from drafting economically protectionist laws and instead, through collaboration and multilateral cooperation, seek common ground with lawmakers in neighboring states that share renewable energy development goals. Policy makers should seek to enact collaborative solutions on scalable levels, such as memoranda of understanding, regional compacts, and/or multinational agreements. Invariably, such cooperation will reduce litigation costs, allow proponents to focus their efforts in a positive manner, and create collaborative policies that will propel renewable energy development forward.

#### Memoranda of Understanding and Regional Agreements

Cooperation and collective action by various interested parties would allow energy development to realize economies of scale, resulting in lower costs to consumers and encourage development in a localized region, rather than in an individual state. Memoranda of Understanding ("MOU") may be a good first step for various public and private stakeholders that seek to create cooperative arrangements. MOUs are typically short documents (3-10 pages) that describe bilateral or multilateral agreements among stakeholders, and express that parties intend

to act on a common course of action. MOUs are used in lieu of legally enforceable agreements, evincing a spirit of cooperation and collaborative resolve.

For example, two federal agencies, the U.S. Department of the Interior (“DOI”) and the Department of Energy entered into a MOU “in order to prioritize and facilitate environmentally-responsible deployment of commercial-scale offshore wind and marine and hydrokinetic (MHK) energy technologies on the Outer Continental Shelf (OCS) through collaborative efforts on issues of mutual interest.” (DOI MOU, 2010). In July, 2010, a collaborative MOU between a the DOI and several states was signed to “Create an Offshore Wind Energy Consortium to Coordinate Issue of Regional Applicability for the Purpose of Promoting the Efficient, Expeditious, Orderly and Responsible Development of the Wind Resources of the Atlantic Outer Continental Shelf.” (Consortium MOU, 2010). The purpose of this MOU was to “facilitate Federal-state cooperation and coordination for the efficient, expeditious, orderly, and responsible development of the significant wind resources of the Outer Continental Shelf along the Atlantic coast through collaborative efforts on issues of mutual interest.” Participants also expressed “their intent to join together in an Atlantic offshore wind energy consortium to undertake collaborative activities and consultation to achieve region-wide strategies and produce specific recommendations to facilitate the development of Atlantic offshore wind resources.” (Consortium MOU, 2010). On the state level, several Mid-Atlantic states signed an MOU in 2009 “Related to Common Interests Associated with Offshore Wind Energy Development.” (DELMARVA MOU, 2009). The parties to this MOU agreed to, among other things, “develop strategies to encourage sustainable market demand for offshore wind power, including state and regional policies and incentives that can be used across state boundaries for the benefit of the industry as a whole.” The MOU encouraged other Atlantic coastal states to join the agreement, and each party agreed to appoint one or more key personnel to develop the collaborative process related to offshore wind. (DELMARVA MOU, 2009). Private companies can enter into MOUs, such as the 2013 agreement entered into by GDF Suez, a French multinational electric utility company, and Newcom, a Mongolian investment company, to build the first wind farm in Mongolia, with a capacity of 50MW. (GDF MOU, 2013).

MOUs also can be signed between nations, as evidenced by the 2012 MOU between India and Malaysia on “Cooperation in Renewable Energy,” which covers biomass, hydropower, solar energy, energy from domestic and agricultural waste, and wind power. (India MOU,

2012). The MOU articulates a desire to “strengthen and further develop cooperation between the two countries in the field of renewable energy” and the belief that “such cooperation would serve their common interest and contribute to the enhancement of the economic and social development of the people of both countries.”

Regional agreements, which are akin to MOU, are cooperative agreements between various states in a region that are seeking to achieve mutual goals and memorialize the agreement to support such action. Any form of regional cooperation has the potential to encourage greater regional investment and job formation, and drive down the cost of renewable energy implementation more efficiently than an uncoordinated and competitive assortment of individual programs.

In June 2009, a significant regional effort was undertaken by five Mid-Atlantic state governors. The Governors of Delaware, Maryland, New Jersey, New York, and Virginia established the Mid-Atlantic Regional Council on the Ocean (“MARCO”) as an intergovernmental organization to facilitate regional coordination and collaboration on a variety of marine issues, including offshore renewable energy development. (MARCO, 2009). The regional agreement is intended to “foster a cooperative and constructive relationship between the States, avoiding unintentional conflicts . . . [and] lead to greater predictability and efficiency in regulatory processes.” (MARCO, 2009). One of MARCO’s four key priorities is collaborating on a regional approach to facilitate offshore renewable energy development, with a primary focus on wind energy, and to develop sustainable offshore renewable energy development within a more predictable, science-based management framework. (ELI MARCO, 2013).

MARCO is managed by the Mid-Atlantic Regional Council on the Ocean (“the Council”), and each state designates a point person to the MARCO Executive Committee. The Executive Committee coordinates the individual state’s activities within various priority areas and implements the Council’s direction. (MARCO, 2009). Further, the Council liaises with federal agencies that have significant resource responsibilities in the Mid-Atlantic, and coordinates contact with point persons from these designated agencies.

MOU and regional agreements can be powerful policy tools in that they can provide opportunities for likeminded stakeholders to memorialize the objectives they are seeking to achieve, and can provide a forum for robust discussion on how best to achieve those goals. MOU and regional agreements can help to ensure that the parties have clarity of purpose, and by

identifying operational, legal, and financial issues while drafting the agreement or MOU, the parties can seek to include a set of measurable objectives and benchmarks for implementation.

Several factors may initially inhibit the creation of a regional agreement or MOU, such as mistrust among the stakeholders and competition to prioritize individual goals. The various parties may have different intentions, which may only become clear after discussions begin. Further, artful drafting will be crucial to attain buy-in by the various stakeholders.

### Regional Compacts

Regional compacts are another mechanism that stakeholders can utilize to create more cooperative agreements. Regional compacts, as opposed to regional agreements and MOU, have more ‘teeth’ because they are typically signed into law by legislators, and may carry Congressional imprimatur. Article I, Section 10 of the U.S. Constitution states that “no State shall, without the Consent of Congress ... enter into any Agreement or Compact with another State.” With this clause, the Framers of the Constitution acknowledged that states acting in concert could pose a potential threat to the new nation, and this prohibition was initially enacted to preclude political alliances among the fledgling states. Later, the Supreme Court ruled that Congressional consent was only required for agreements between states that tend to increase the state’s respective political powers, and encroach on federal supremacy. (Steel Corp., 1978). While Congressional ratification is no longer a requirement for regional compacts, ratification gives a compact permanence and legitimacy which allows member states to enjoy that their mutual participation in such a compact is safeguarded against federal preemption.

Regional compacts can involve any subject matter, and have been successfully implemented for management of joint resources. An example of successful collaboration is the Delaware River Basin Compact (“DRBC”), which is between Pennsylvania, Delaware, New Jersey, and New York. (Collier, 2007). Policymakers from the various states drafted laws and signed the compact legislation into law in 1961, and the signing of the DRBC marked the first time since the nation’s birth that a group of states joined together as equal partners in a planning, development and regulation of a resource. The DRBC further demonstrates that five separate governmental bodies with their own sovereign powers can successfully work together on an equal footing in managing a common resource. (DRBC, 2013). The DRBC created a regional

body with the force of law to oversee a unified approach to managing a river system without regard to political boundaries, and addressed interstate water issues before they reached a crisis. The commission of the DRBC was given broad authority to plan, regulate and coordinate management of the basin's waters. The style of management was an adaptive management approach, which vested members with authority to modify terms of decree upon unanimous consent. (Collier, 2007; DRBC, 2013).

Another example of a successful regional compact is the Port Compact of 1921 which established the Port Authority of New York and New Jersey ("Port Authority"). (Columbia, 2012). In 1917, the governors of New York and New Jersey appointed a bi-state commission to address issues with port and harbor coordination between the two states. The commission recommended that the two states work collaboratively, and the Port Authority was ultimately established in order to cooperatively resolve disputes and address issues concerning boundaries, marine police jurisdiction, and freight rates. The authority is run by twelve unsalaried commissioners, and governor of each state appoints six members of the Board of Commissioners, subject to state senate approval. (Columbia, 2012; Port Authority, 2014). An Executive Director is appointed by the Board of Commissioners, and is responsible for managing the operation of the Port Authority in a manner consistent with the agency's policies, as established by the Board. The Port Authority undertakes projects and activities in accordance with the Port Compact in 1921, and amendatory and supplemental legislation. (Port Authority, 2014). The Port Authority is considered highly successful, and has produced a modern and efficient system of bridges, tunnels, and terminal facilities without adding to the burden of the New York or New Jersey taxpayers. (Columbia, 2012).

Regional compacts are beneficial in that they provide greater certainty to the participants than a MOU and they avoid the problems with the dormant Commerce Clause. Since compacts carry the force of law, participants are protected against unilateral withdrawal or lax participation by one member state. The makeup of a regional compact allows member states to centralize authority into a unified regulatory body, and by design, can have a transparent code of conduct and decision making. Participation in a regional compact would enhance policymaking capacity for the member states by allowing participants to work cooperatively to promote a common agenda. A further benefit of a regional compact is that it signals a serious commitment to

investors, and may allow the participants to pool resources to achieve market efficiencies. (Stiles, 2009).

In order to extract mutual benefits from a regional compact, participants should enter seek to enter into agreements out of necessity, but should enter into such binding agreements voluntarily. In order to avoid market failures and facilitate the development of a regional agreement, it may be necessary to develop an institution or regional body through which the agreements are negotiated. (Devlin, 2002). This institution could help participant states remove barriers to mutually advantageous collective actions, and could facilitate cooperative efforts by overseeing the regional agreements and by coordinating multilateral policies on a micro and macro level. (Devlin, 2002). In order to efficiently integrate economically, the participant states should cooperate systematically to administer a regional agreement to save in development costs. The individual states can coordinate actions through a binding regional agreement, which should create cooperative effects in order to realize mutual advantages. (Devlin, 2002).

There are downsides to regional compacts, however, such as political dissidence among the various participants, exclusion of non-member states and competition among states. Moreover, drafting the terms of a regional agreement is an onerous task, and policy makers will need to conceptualize and develop additional regional projects that incentivize cooperative development of green technologies. While stakeholders may be theoretically interested in drafting such a cooperative agreement, in order to effectively cooperate, there will invariably be some form of subordination of the members' sovereignty to the interests of the group. (Devlin, 2002). It would be antithetical to the cooperative spirit for individual stakeholders to expect that each party's individual goals would be given priority over a group or common goal.

In order to successfully implement a cooperative agreement, a compact must be drafted in a way that allows the participants to achieve important individual goals, such as meeting RPS standards and job creation, as well as achieving a common goal, such as mitigation of the effects of climate change. Although each participant may not fully actualize each individual or common goal, the objective of the regional agreement for participants who want to develop renewable energy would be to work cooperatively to find solutions that maximize the overall benefits of the stakeholders, lead to positive collaboration, and do not lead to counterproductive exclusionist actions and costly litigation.

Moreover, participants in a regional compact may be able to enact in-region location eligibility requirements, which are more likely to withstand constitutional challenge than in-state location requirements. (Elefant, 2011). While regional location requirements are still somewhat problematic under the Commerce Clause, these policies would be less likely to attract litigation because regional eligibility requirements would be far less restrictive, practically and geographically, than in-state location requirements. Moreover, while in-state location requirements have been overruled by courts on Commerce Clause grounds for many years, there are no cases that specifically address the constitutionality of in-region location requirements. (Elefant, 2011). For these reasons, while an in-region location requirement is not free of constitutional concerns, regional policies provide a less risky approach to RPS eligibility than in-state location requirements. (Elefant, 2011).

### Multinational Agreements

Lawmakers from various countries who may be interested in working collaboratively may choose to enter into freer trade agreements. Although a key rule of the WTO system is that reductions in trade barriers should be applied on an MFN-nation basis to all WTO members, and that no WTO member should be discriminated against by another member's trade regime, regional trade agreements ("RTA") are an important exception to this rule and are permitted under the WTO. In an RTA, reductions in trade barriers apply only to the parties to the agreement. (DFAT, 2013). RTAs must be consistent with the WTO rules governing such agreements, which require that parties to an RTA must have established free trade on substantially all trade within the regional area, and that the parties cannot raise their tariffs or other barriers against countries outside the agreement.

In addition to RTAs, stakeholders have been lobbying policy makers to consider other free trade options to defeat protectionism in the wind sector. The European Wind Energy Association has been lobbying the European Commission to recognize international opportunities for discussion of the elimination of tariffs and non-tariff barriers to wind and other renewable energy sources. The wind industry has been working with turbine manufacturers to promote the adoption of policies such as Sustainable Energy Free Trade Areas ("SEFTA") or an Environmental Goods and Services Agreement ("EGSA"), both of which are policies that offer, among other measures, free trade in renewable energy technologies. (Baillie, 2011). Industry



representatives and manufacturers, such as General Electric and Vestas, have begun discussion on opening up “trade in technologies and services that support the fight against climate change,” and “support an EGSA that lowers tariffs and opens up markets.” (Baillie, 2011). Likewise, if governments commit to removing or substantially lowering the costs imposed on environmental goods and services, the removal of these barriers could provide an important opportunity for growth in the renewable energy industry.

### **Collaborative Solutions Will Propel Renewable Energy Development Forward**

Cooperation is crucial in order to achieve mutually beneficial goals, create market efficiencies, and propel renewable energy development forward. A critical component of any cooperative agreement is that each party perceives the partnership as beneficial, and that the collaborative process creates favorable outcomes for each party. Collaboration should support the growth of a burgeoning industry, and propel the industry forward, rather than creating roadblocks and obstacles for parties that are seeking to achieve the same goals. Notably in the two cases discussed herein, all of the various stakeholders were seeking to develop renewable energy, yet their disputes had a chilling effect on renewable energy development. These disputes highlight the critical need to limit oppositional actions and enact policy alternatives among stakeholders who support development of renewable energy.

While there is no one-size-fits-all answer to encourage collaborative development, a functioning cooperative union should seek to strike a balance between the legitimate interests of stakeholders and keeping costs at a minimum to encourage ratepayer buy-in and public support for renewable energy development. In order to develop effective cooperative action on climate change, it will be necessary to further research, analyze, and develop collaborative efforts and encourage stakeholders to seek to make positive mutual progress rather than expend resources in counterproductive activities, such as disputes in the WTO and Commerce Clause litigation. Such inimical actions have ultimately forestalled direct progress on renewable energy development to the detriment of all those who view renewable energy development as an essential element to solving issues related to climate change.

The policy prescriptions described in this paper can be considered an important instrument for achieving the policy objective of developing more renewable energy sources. These tools are clearly not the only available instruments for achieving this goal, but by utilizing these

mechanisms, along with other collaborative policies and legally defensible laws, proponents of will be better suited to attain the ultimate goal of fostering renewable energy development.

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