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Carbon Prices: Should They Be Incorporated Into FERC-Related Wholesale Electricity Markets?

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On April 13, 2020, a broad group of trade associations, power producers, and other stakeholders filed a request asking the Federal Energy Regulatory Commission (FERC or Commission) to hold a technical conference or workshop to discuss integrating state, regional, and national carbon pricing in FERC-regulated wholesale electric energy markets. There is no deadline for FERC to act on the request, and no requirement that it act.

If FERC takes up the request to consider carbon pricing, it would be a first for the Commission, which regulates the transmission and wholesale sale of electricity, but generally does not have oversight of environmental matters for power producers, except at hydroelectric plants. The stakeholder group is not asking FERC to direct implementation of a carbon-pricing mechanism, or institute a rulemaking proceeding, but rather gather a range of stakeholders to discuss technical and implementation issues related to incorporating carbon-pricing policies into the wholesale organized markets. Some believe that integration of carbon price signals could increase the competitive profile of lower- and zero-emission resources in electricity markets.

FERC-jurisdictional wholesale markets are generally operated by Independent System Operators (ISOs) and Regional Transmission Organizations (RTOs) that determine which generators should run at any given time based on cost. Put simply, the ISOs and RTOs determine how much generation is necessary to meet demand as it changes throughout the day, and dispatch the lowest-cost generators that can meet that demand.

The requesting parties ask FERC to examine potential state, regional, or national carbon pricing mechanisms and how those carbon prices could be, or already are, incorporated into wholesale market pricing and dispatch decisions. The examination could include consideration of existing regional carbon price mechanisms (i.e., the Regional Greenhouse Gas Initiative (RGGI) and California-Quebec cap-and-trade market), as well as individual state carbon-pricing mechanisms.

Certain wholesale electric energy and capacity markets have been grappling with how to reconcile wholesale markets with state carbon-reduction policies for some time. This has bearing on FERC's jurisdictional scope, such as how these markets function and determination of prices. The request notes that the California Independent System Operator (CAISO) already incorporates carbon prices from California's cap-and-trade program into its Electricity Imbalance Market (EIM), a mechanism for supplying and dispatching electricity to balance fluctuations in generation and load. CAISO has already placed a carbon adder on bids coming into California from other states that are not subject to California's cap-and-trade program.

Other market operators have adopted tariff mechanisms to incorporate, or already have bidding structures in place that allow for consideration of compliance costs arising out of state carbon regulations in the wholesale markets they run. In addition, the New York Independent System Operator (NYISO) has developed a complete market design for introducing a carbon price into its wholesale electricity market which it has identified as the most efficient mechanism to implement the state's public policy initiatives to combat climate change, and continues to actively work with state entities, industry representatives, and other parties to advance. The NYISO has committed to its stakeholders it will participate in this effort if a technical conference is held. The CEO of ISO New England (ISO-NE) has also publicly voiced support for a carbon price; and the PJM Interconnection (PJM) has conducted a study on carbon pricing and how it could incorporate a carbon price in some PJM states in a manner that allows it to avoid leakage (emissions shifted from one market with a carbon price to another without a carbon price).

In recent decisions, FERC Commissioners have split on the extent to which FERC is required to evaluate and consider a project's contribution to climate change under the Natural Gas Act and the National Environmental Policy Act, and the current Commission may or may not grant this request for a technical conference. However, it is apparent that an increasing number of stakeholders and policymakers are becoming interested in how carbon price signals are incorporated into wholesale electricity markets. Increased integration of carbon price signals into wholesale electricity markets may make low carbon generation more economically attractive, while raising the costs of higher-emitting resources.

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