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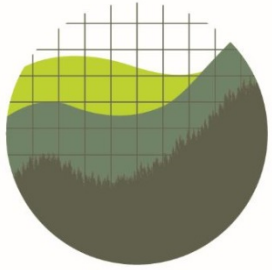
Carbon Pricing in RTO Markets: Jurisdictional Considerations

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PJM Carbon Pricing Senior Task Force



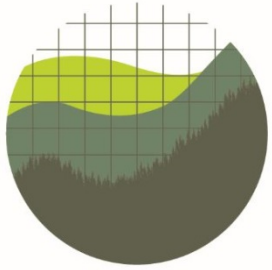
Legal Principles

Federal Requirements

- FERC approval required for “rules and regulations affecting or pertaining to” rates
- RTO rules must not regulate activity explicitly reserved to the states
- The change must result in just and reasonable rates
- The change must not result in undue preference or discrimination
- Factual findings must be supported by substantial evidence

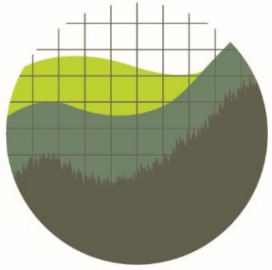
State Requirements

- States may not establish or “replace” a wholesale rate
- Dormant Commerce Clause (DCC): Any state policy components must be directed at legitimate policy goals that are unrelated to protectionism



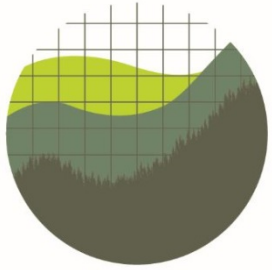
Overview of “Carbon Pricing” Paths

- “Carbon pricing in PJM” can mean different things
- Can divide approaches into 3 potential paths based on the legal authority supporting the carbon price
 - RTO-implemented carbon price (optionally with state opt-in)
 - Recognize PJM has stated it does not intend to impose a carbon price
 - State-implemented carbon price with corresponding changes to PJM tariff to allow cost-recovery and facilitate emissions accounting
 - A hybrid-approach: State-implemented carbon price on in-state generators with RTO-implemented border adjustment



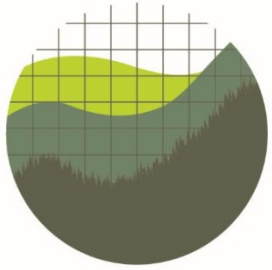
RTO-Implemented Carbon Price

- Academics have put forward a number of potential legal theories under which FERC can approve a carbon price explicitly incorporated into RTO markets
 - Improving wholesale market efficiency is a critical component of just and reasonable rates
 - Bethany Davis Noll & Burcin Unel, *Markets, Externalities, and the Federal Power Act: The Federal Energy Regulatory Commission's Authority to Price Carbon Dioxide Emissions*, 27 N.Y.U. ENVTL. L.J. 1 (2019)
 - Environmental costs are a permissible consideration when evaluating just & reasonable rates
 - Christopher J. Bateman & James T. B. Tripp, *Toward Greener FERC Regulation of the Power Industry*, 38 HARV. ENVTL. L. REV. 275 (2014)
 - A carbon price can “rationalize” or “harmonize” the outcomes that various state policies aim to achieve in a way that is consistent with wholesale market design
 - Ari Peskoe, *Easing Jurisdictional Tensions by Integrating Public Policy in Wholesale Electricity Markets*, 38 ENERGY L.J. 1 (2017)
 - ROMANY WEBB & JUSTIN GUNDLACH, COLUMBIA LAW SCHOOL SABIN CENTER FOR CLIMATE CHANGE LAW, CARBON PRICING IN NEW YORK ISO MARKETS: FEDERAL AND STATE ISSUES (2017)
 - A carbon price will break down participation barriers for non-carbon resources and limit undue discrimination
 - Joel B. Eisen, *FERC's Expansive Authority to Transform the Electric Grid*, 49 U.C. DAVIS L. REV. 1783 (2016)
- Specific legal theory will influence permissible market design details



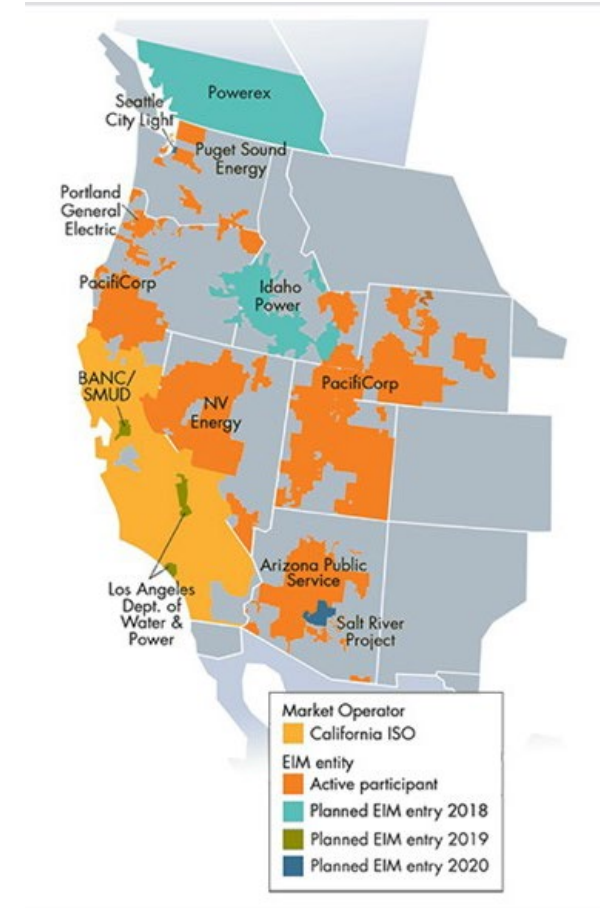
RTO-Implemented Carbon Price

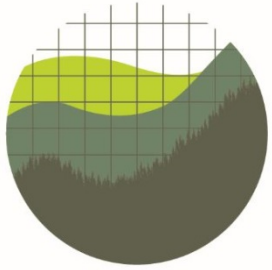
- Key Issue: State opt-in
 - FERC is not required to assert jurisdiction, particularly when there are complicated jurisdictional questions at heart of federal/state divide. *New York v. FERC*, 535 U.S. 1 (2002)
 - Orders 719-A and 745 provide precedent that an opt-in may be permissible even when FERC determines that a market change is just and reasonable
- Key Issue: State involvement in selection of carbon price
 - Carbon price bundled into wholesale sale is FERC jurisdictional. *WSPP*, 139 FERC ¶ 61,061 at P 23 (2012)
 - States cannot replace a FERC jurisdictional rate. *Hughes v. Talen*, 136 S. Ct. 1288, 1293 (2016)
 - So, RTO will have responsibility to explain why the rate is just and reasonable. But that does not prohibit it from pointing to state policies or proceedings to support the RTO's legal theory
- Key Issue: Undue Discrimination
 - Rules affecting rates cannot unduly discriminate or give undue preference
 - Cannot treat similarly situated resources differently; cannot treat differently situated resources the same
 - DCC is a limit on state, not federal action, so will not generally apply to FERC-approved tariff provisions



State-Implemented Carbon Price

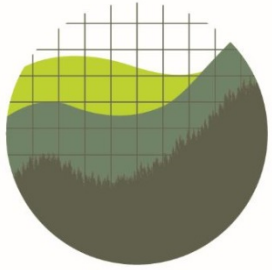
- Just and reasonable rates are rates produced by competitive markets where resources have the opportunity to recover their costs
 - FERC has long recognized costs can include environmental compliance costs such as cap-and-trade allowance costs
 - Order No. 579, 60 Fed. Reg. 22,257 (1995)
- Tariff adjustments by PJM may be needed to attribute emissions to electricity imports and to give resources a mechanism to include compliance costs in bid parameters
 - FERC precedent suggests that such adjustments can be just and reasonable
 - FERC approved CAISO revisions implementing CA application of carbon price to imports attributed to EIM least-cost dispatch algorithm
 - 147 FERC ¶ 61,231 at P 238 (2014)





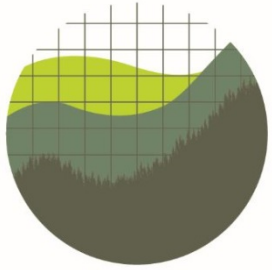
State-Implemented Carbon Price

- Key Issue: Under this pathway *state law* must impose the cost. Do states have authority?
 - All RGGI states impose costs on in-state generators
 - Some states **may** already have authority to implement price on imports
 - **New Jersey** Global Warming Response Act and RGGI Law require BPU to develop a regulatory mechanism to mitigate leakage. N.J. Stat. Ann. § 48:3-87(c)(2)
 - **Maryland** Greenhouse Gas Emissions Reduction Act mandates a plan to reduce statewide greenhouse gas emissions, including emissions from delivered electricity. Md. Code Ann., Envir. §§ 2-1205(a), 2-1202(h)
 - Other states could adopt provisions for import/export adjustments
- Key Issue: Dormant Commerce Clause
 - This is an issue of state law construction, not PJM's implementation
 - DCC not violated if state laws provide equal treatment to similarly situated products (in-state generation, imports, exports)
 - Programs that look at actual environmental harm for both in-state product and imports have been upheld
 - *Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070, 1089 (9th Cir. 2013); *Allco v. Klee*, 861 F.3d 82 (2nd Cir. 2017)
 - DCC concerns may require a mechanism for resources to opt-out of participating in the state program
 - 153 FERC ¶ 61,087 at P 55 (2015)



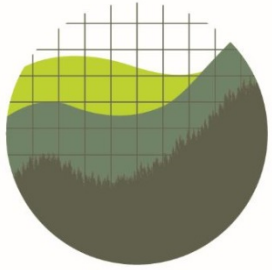
Hybrid Approach: State-Implemented for In-State, RTO-Implemented Border Adjustment

- Untested and not fully discussed in the academic literature
- RTO would need to explain why a border adjustment is just and reasonable and not unduly discriminatory given state-imposed carbon price on in-state generators
- Could draw on the legal theories discussed for RTO-implemented approach



Takeaways

- Carbon pricing means different things:
 - Helping to implement state application of carbon price on electricity imports (and crediting of exports)
 - Implementing a carbon price under the Federal Power Act (potentially with state opt-in)
- “Carbon pricing” is legally viable
 - FERC has already approved RTO tariffs that reflect costs of state-implemented carbon pricing, and that facilitate attribution of imports
 - A number of legal theories suggest an RTO-implemented carbon price (potentially with state opt-in) is consistent with Federal Power Act requirements
 - Design details should flow from legal justification
- Each approach involves distinct legal requirements that can be addressed through appropriate policy design and legal justification



Thank You!

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