

INSIGHTS

FERC Issues Carbon Pricing Policy

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On April 15, 2021, the Federal Energy Regulatory Commission (“FERC” or “Commission”) issued its much anticipated policy statement on carbon pricing in organized markets.^[1] The non-binding policy statement provides guidance regarding the manner in which FERC will evaluate proposals submitted pursuant to Section 205^[2] of the Federal Power Act (“FPA”) to establish market rules for incorporating a state-determined carbon price into organized markets operated by Regional Transmission Organizations and Independent System Operators (“RTO”).

In the policy statement, FERC observes that RTOs are increasingly evaluating incorporating carbon pricing into their wholesale market in response to state programs that seek to reduce greenhouse gas (“GHG”) emissions through the imposition of fees associated with emissions and cap-and-trade programs. Acknowledging that the incorporation of a state-determined carbon price into wholesale markets has the potential to efficiently incorporate state public policies into RTO markets, the Commission explains that it is “the policy of this Commission to encourage efforts of [RTOs] and their stakeholders—including States, market participants, and consumers—to explore and consider the value of incorporating state-determined carbon prices into [RTO] markets.”^[3]

The Commission emphasizes that the policy statement is not intended to express a “preference for a state-determined carbon pricing approach over other state policies” but is only intended to encourage discussions at the RTO level given the potential benefits of carbon pricing.^[4] In order to help guide RTO efforts, the policy statement provides non-binding guidance regarding how the Commission plans to evaluate proposals to incorporate a state-determined carbon price in wholesale markets.

As a threshold matter, the Commission affirmed that wholesale market rules that incorporate a state-determined carbon price into RTO markets “can fall within the Commission’s jurisdiction as a practice affecting wholesale rates” subject to the Commission’s jurisdiction under Section 205 of the FPA.^[5] The Commission observed that “wholesale market rules that incorporate a state-determined carbon price could . . . govern how resources participate in the [RTO] market, how market operators dispatch those resources, and how those resources are ultimately compensated.”^[6] The Commission also found that wholesale market rules that incorporate a state-determined carbon price would neither implicate matters that had been reserved exclusively to the states pursuant to the FPA nor displace state authority over generation facilities or other matters.

While the policy statement acknowledges that any filings proposing market rules to incorporate a state-determined carbon price would be approached on a case-by-case basis, the policy

statement provides guidance regarding the types of considerations that the Commission would take into account when evaluating a proposal by an RTO to incorporate a state-determined carbon price into wholesale markets. Those considerations are:

- How, if at all, do the relevant market design considerations change depending on the manner in which a state or states determine the carbon price (e.g., price-based or quantity-based methods)? How would state-determined carbon prices, including any changes to these prices, be reflected in RTO/ISO tariffs or market designs?
- How would the FPA section 205 proposal provide adequate price transparency and enhance price formation?
- How would the carbon price or prices be reflected in locational marginal prices (LMP)?
- How would the incorporation of the state-determined carbon price into the RTO/ISO market affect dispatch? Would the state-determined carbon price affect how the RTO/ISO co-optimizes energy and ancillary services? Would any reforms to RTO/ISO co-optimization rules be necessary in light of the state-determined carbon price? Would any reforms to other market design elements be necessary, such as to market power mitigation rules or other rules that affect whether the market produces just and reasonable rates?
- Would the filer's proposal result in economic or environmental leakage? If so, how might the proposal address any such leakage?
- What elements of the proposal affect the wholesale rates paid by customers? How does the proposal consider this impact and the impact on consumers overall?[\[7\]](#)

While each of the commissioners voted to approve the policy, both Commissioner Danly and Commissioner Christie issued separate concurrences and dissents expressing concern about aspects of the policy statement. Commissioner Danly wrote separately to emphasize that the policy statement stands for nothing more than the proposition that the Commission is obligated to “entertain” proposals to incorporate state carbon pricing policies, and to dissent from the policy statement to the extent that it attempts to prejudge the jurisdictional merits of any future Section 205 proposals.[\[8\]](#) Similarly, Commissioner Christie stated that while he supported the statement to the extent that it affirms that the Commission will entertain proposals filed under Section 205, he was dissenting to the extent that the policy statement appeared to invite proposals for carbon pricing that are inconsistent with the following principles:

- Carbon pricing is nothing more than a euphemism for a carbon tax.
- FERC does not have the authority to impose a carbon tax absent a decision by Congress to amend the FPA to give the agency that authority.
- FERC does not have authority to approve a proposal by an RTO to impose a carbon tax, as RTOs were created by FERC and are quasi-governmental in nature.

- FERC may, however, allow an RTO to recognize a carbon tax imposed by a state authority.
[\[9\]](#)

Importantly, the policy statement does not require any RTOs to take any steps to adopt a state-determined carbon price into its markets. Nevertheless, the policy statement is notable in that it expressly encourages RTOs to work with stakeholders to consider incorporating carbon pricing into their markets. The policy statement also provides additional certainty to RTOs regarding the Commission's view of its own authority to evaluate carbon pricing measures and the types of issues that the Commission expects RTOs to address in any filings proposing such measures.

[\[1\]](#) *Carbon Pricing in Organized Wholesale Electricity Markets*, 175 FERC ¶ 61,036 (2021) ("Statement").

[\[2\]](#) Codified at 16 U.S.C. § 824d.

[\[3\]](#) Statement at P 11.

[\[4\]](#) *Id.* at P 19.

[\[5\]](#) *Id.* at P 12.

[\[6\]](#) *Id.* at P 14.

[\[7\]](#) *Id.* at P 21.

[\[8\]](#) *Carbon Pricing in Organized Wholesale Electricity Markets*, 175 FERC ¶ 61,036 (2021) (Danyl, Comm'r, concurring in part and dissenting in part).

[\[9\]](#) *Carbon Pricing in Organized Wholesale Electricity Markets*, 175 FERC ¶ 61,036 (2021) (Christie, Comm'r, concurring in part and dissenting in part).