

OPINION

The looming threat to state renewable goals in wholesale electricity markets

By Jessica Bell

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The following is a contributed article by Jessica Bell, Clean Energy Attorney in the State Energy & Environmental Impact Center at NYU School of Law.

While I certainly agree with Michael Hogan's affirmation of states' rights to address environmental externalities through energy policy in his recent Utility Dive opinion piece, "States' rights, states' wrongs," his argument omits the important discussion of wrongs by Regional Transmission Operators (RTOs) and Independent System Operators (ISOs).

Specifically, several RTOs have undertaken a misplaced and unevenly applied mission to scrub the impacts of state policies from markets. States' rights to determine resource mix are now on a dangerous collision course with organized wholesale markets. And it is not the states that need to correct course.



In litigation over Illinois' Zero Emission Credit program, the Federal Energy Regulatory Commission (FERC) agreed that the program is not preempted by federal law, but noted its own authority to "confront" the effects of these (and other) state programs on wholesale electricity markets.

In practice, FERC's approach has created uncertainty for generators, consumers and other stakeholders. In a recent example, the inability of Vineyard Wind's historic offshore wind project — procured pursuant to state directive — to fully participate in the ISO-New England capacity market, frustrated state policy priorities and cost ratepayers an estimated \$270 million.

For states, many of which are setting more and more ambitious clean energy goals, the stakes are high.

Recent reports have highlighted the threat of climate change. Many states have been working on adaptation plans to attempt to mitigate some of the impacts of climate change on their citizens and property.

But states are unfortunately encountering additional obstacles to their clean energy goals as renewables and other zero-emission resources are shut out of wholesale electricity markets. This

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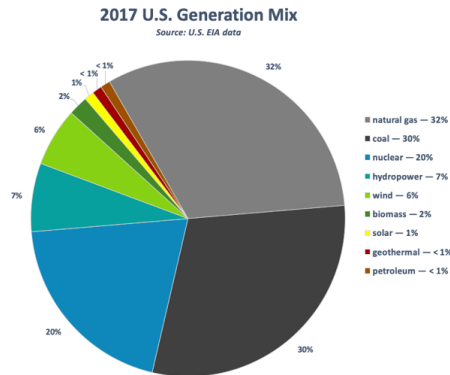
fundamental bias undermines state efforts and puts more costs onto ratepayers.

Power generation in the U.S.

The electric power sector is one of the top two greenhouse gas emitting sectors in the U.S., accounting for 28% of total 2016 emissions. Transportation is the other top-emitting sector in the U.S., and efforts to reduce these emissions require a robust, clean grid.

Coal combustion is the most carbon intensive fuel source: In 2016, coal contributed about 67% of CO₂ emissions for the electric power sector, but only generated about 32% of the electricity.

The following chart shows the contribution of different fuel types to total generation in the U.S. in 2017.



Subsidies, distortions and other dirty words

States make decisions over generation resource mix in accordance with the Federal Power Act. The Supreme Court in *Hughes* recognized and preserved this balance between the states' historical and important role in regulating generation facilities and FERC's authority over wholesale markets.

Hughes faulted a Maryland program for tethering its encouragement of new generation to participation in the wholesale market. But the Court recognized the numerous, permissible (under the Federal Power Act and the U.S. Constitution) ways that states could "encourage the development of new or clean generation." And subsequent caselaw has found that states can craft such programs without an impermissible tether.

The problem now is not state programs that tie to wholesale market participation, but rather wholesale markets that cannot interface with state clean energy programs. Many RTOs/ISOs run a capacity market to procure resources to meet future demand.

These markets, conducted as advance auctions, are designed to provide price signals to generators, and their rules are subject to

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frequent revision in an effort to get the signals right.

However, these signals are skewed toward investment in new fossil fuel-fired generation. As states move towards more renewables and away from fossil fuels, conflicts between the signals from the market and the signals from the states correspondingly increase.

This creates a collision course between state preferences for cleaner energy that are based, in part, on a recognition that fossil fuels carry a carbon burden unaccounted for in the wholesale market. And the more that states ramp up their clean energy goals, the more severe the impact at the intersection.

For example, a divided FERC attacked state clean energy preferences by concluding that they are a form of "out-of-market" support, and the current market rules "fail[s] to protect the integrity of competition in the [PJM] wholesale capacity market against unreasonable price distortions and cost shifts caused by out-of-market support."

Commissioner Glick dissented. He pointed out that FERC's action tramples on "the states' exercise of the exclusive authority that Congress has reserved to them[.]"

FERC needs to abandon the notion that clean energy preferences represent an inappropriate "out-of-market" distortion.

As state attorneys general have pointed out, state clean energy preferences reflect a market *correction* by accounting for the carbon costs embedded in fossil fuel use. And if FERC or RTOs are serious about cataloging out-of-market factors, they cannot single out state clean energy preferences while ignoring federal and state fossil fuel subsidies that have long provided out-of-market benefits to coal and gas suppliers.


(For example, Pennsylvania exempts oil and gas production from local property taxes.)

A one-two punch for states' rights, the environment and public health


FERC's manipulation of interstate electricity markets to penalize clean energy resources preferred by many states is unduly discriminatory.

In another recent case, FERC failed to act in order to accommodate the participation of Vineyard Wind's offshore wind project in the ISO-New England capacity market.

As I noted earlier, the estimated price tag of this exclusion was \$270 million in lost ratepayer savings, according to the New England Power Generators Association, although they characterized it as an "impact (harm) to all capacity suppliers". It drew criticism from Attorney General Maura Healey as well as

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FERC Commissioners LaFleur and Glick, who said that everyone involved "deserve[d] better."

But the damage extends further.

As state-driven renewable buildout is jeopardized in both the short term and long term by federal action (and inaction), states still must confront the devastating impacts of climate change. These realities include increased flooding, fires and severe weather events, as well as direct health impacts, such as higher asthma rates.

States must continue to push back against federal intrusion on their Federal Power Act rights, in addition to rollbacks of regulation of the nation's top CO₂ emitters, to counter this multi-frontal attack on human health and the environment.

Aligning markets with state policy preferences


Frequent revisions to capacity market rules to try to correct for alleged "distortions" lead to uncertainty. The PJM proceeding discussed above remains unresolved, leaving PJM to determine how to approach upcoming auction deadlines when FERC found the current rules to be unjust and unreasonable, but has not yet acted on a replacement. This uncertainty benefits no one.

The current path erodes states' rights and views cleaner generation as a nuisance that undermines the market, rather than as a valued participant. And continuing this way could ultimately become much more disruptive to markets if states deem more drastic measures necessary to control in-state resource development.

As long as federal environmental and energy policy declines to take seriously the need to reduce carbon emissions and recognize the monetary benefits of doing so, this dissonance will only grow.

States and RTOs/ISOs should work with other stakeholders to develop and implement market changes that respect the role of states under the Federal Power Act in determining generation mix. RTO markets should accommodate state policies to internalize the externality of carbon emissions, rather than work against them.

This would reduce the conflict between state clean energy preferences and the markets. It is time for decisive action that recognizes that addressing climate change and the social costs of carbon pollution is a correction and not a distortion.

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