

ACE-NY RELEASES REPORT ON CARBON PRICING IN LATEST PUSH FOR NYISO WHOLESALE MARKET REFORM

Hodgson Russ Renewable Energy Alert
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Developers, builders, and financiers of renewable energy and energy storage projects in New York, even those of distributed energy resources, should closely monitor the ongoing New York Independent System Operator (NYISO) Carbon Pricing proceeding and consider its impact on investment strategy and future revenue streams – especially given wholesale market prices’ inclusion in the Value of Distributed Energy Resources (VDER) tariff “value stack.” Last week, the Alliance for Clean Energy New York (ACE-NY) published *Building Clean Energy in New York: The Case for Carbon Pricing at the NYISO*, the latest report calling on New York to enact the NYISO-proposed carbon price. This builds upon a growing group of studies, including the Analysis Group’s October 2019 report, which concluded that a carbon price would lower the cost of achieving New York’s aggressive climate goals by a net present value of \$280–850 million between 2022 and 2040.

The recently-enacted Climate Leadership and Community Protection Act (CLCPA), which calls for New York to achieve 70% renewable electricity by 2030, 100% emission-free electricity by 2040, and economy-wide carbon neutrality by mid-century, has added additional impetus for the consideration of a carbon-pricing mechanism. The measure’s proponents contend that it would internalize the costs of the State’s carbon emissions, thus enabling the State to reach its goals more effectively when combined with New York’s Clean Energy Standard and other sector- and industry-specific incentives.

1. NYISO’s Carbon Pricing Proposal

As described [here](#), NYISO’s proposal would introduce a carbon price (\$/ton of CO₂) into New York’s competitive wholesale electricity markets. The carbon price would equal the social cost of carbon, as determined by the New York Public Service Commission (Commission), with adjustments for amounts paid under the Regional Greenhouse Gas Initiative, a cap-and-trade system in which New York participates. The price would only cover carbon dioxide emissions, not other greenhouse gasses such as methane, or local pollutants such as particulate matter.

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In its Day-Ahead and Real Time electricity markets, NYISO collects offers from generators to provide a certain amount of electricity at a certain price (\$/MWh) over a given time period (e.g., 1:00 to 2:00pm). [1] Starting with the lowest priced-offer, NYISO accepts increasingly higher-priced offers until it has secured enough electricity supply to meet the demand for that particular time period. All generators with accepted offers receive the marginal price, known as the “Locational Based Marginal Price” or LBMP. The LBMP is a \$/MWh value representing what it would cost to provide the next additional megawatt at a specific location on the grid. In other words, even if a renewable generator offered to provide electricity for free for a particular hour, it still receive the market-clearing price.

NYISO’s carbon pricing proposal would apply a charge to fossil fuel-based generators for their carbon emissions and the generators would incorporate this charge into their offers to provide electricity. The carbon charge, essentially, would force carbon-emitting generators to provide higher electricity bids to cover this CO₂-related charge. Whenever a carbon-emitting resource was on the margin and set the price, the LBMP would be higher as a result. When this happens, zero or low carbon generators would receive higher market revenues, while fossil fuel generators would have these revenues offset by carbon charges related to their emissions.

To avoid leakage or providing out-of-state resources an advantage over in-state resources, imports and exports will maintain the status quo. Under the carbon pricing scheme, both renewable and fossil fuel imports would earn the LBMP at the relevant border without any “carbon effect.” The lower price thus would not incentivize emission reduction beyond New York, but it also avoids shifting production to non-New York resources that are more costly and likely higher-emitting. As NYISO puts it, the aim is “to apply carbon charges to external transactions such that they compete with internal resources (and each other) as if the NYISO was not applying a carbon charge to internal suppliers.” [2]

Finally, the NYISO would return amounts collected from the carbon charge to the load serving entities (i.e., utilities and energy service companies) that purchase the electricity on behalf of consumers. In this way, the reimbursements would help compensate customers and reduce any carbon-price related increases on their electricity bills.

2. ACE-NY’s Report

In its paper, ACE-NY argues that implementing a carbon price in the NYISO wholesale market would set an example for the rest of the United States of how carbon policy can align with markets and increase the likelihood that the CLCPA’s ambitious state goals actually will be achieved. According to ACE-NY, the initiative would lower costs that otherwise would be paid by the New York State Energy and Research Development Authority (NYSERDA) and other state entities, and reduce the amount of funding needed for transmission investments. With New York State support, the NYISO would be able to implement the carbon price initiative quickly and in a cost efficient manner. Noting that previous New York State renewable energy goals (25% by 2012; 30% by 2015) were not successfully achieved, ACE-NY argues for a “belt and suspenders” approach, with NYISO carbon pricing complementing an existing suite of state policies designed to decarbonize the grid.

ACE-NY observes that carbon pricing will support pre-2015 wind and small-scale hydropower projects that are ineligible for renewable energy credits (RECs) with increased revenues from the wholesale markets. It will also increase the economic gains of building transmission to connect low carbon generation to congested load centers. Implementation of the carbon price would also reduce the cost of the zero-emission credit (ZEC) program that supports New York’s upstate nuclear

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facilities.

The carbon pricing scheme would bring the federally-regulated wholesale markets more in line with state environmental goals, and in so doing, better protect against the possibility of the Federal Energy Regulatory Commission (FERC) intervening to mitigate the effect of out-of-market State actions on wholesale prices, through expansion of buyer-side mitigation, minimum offer price rules, or some other mechanism. According to a recent study by Grid Strategies, NYISO's use of a minimum offer price rule results in procuring excess capacity, costing \$84 million annually, and if fully implemented, \$14 to \$24.6 billion over the next decade. By addressing the absence of a price on carbon in the NYISO market, and more completely incorporating external costs and impacts in market outcomes, there will be less effect on wholesale market prices due to New York's clean energy policy.

Notably, the NYISO carbon pricing initiative dovetails with the ongoing discussion of Indexed RECs as part of the Clean Energy Standard proceeding. The Commission noticed for comment a petition filed by ACE-NY and the American Wind Energy Association seeking to implement an Indexed REC procurement mechanism in place of the current REC structure. NYSERDA currently provides a fixed price for each REC for the life of the contract. Under the proposed mechanism, NYSERDA would procure RECs the value of which would fluctuate in relation to an index of wholesale energy and capacity prices. According to the petitioners, this would avoid a potential "double payment" to renewable generation projects, in the event the NYISO implements a carbon pricing methodology that increases wholesale energy prices. The petition's comment period closed in November. The matter is currently pending before the Commission, and will no doubt be considered as the Commission undertakes the proceeding required by CLCPA to reach 70% renewable energy resource procurement in New York State by 2030.

3. Regulatory Hurdles and 2021 Target Launch

With the findings of the NYISO report published in October, the proposal awaits approval by the NYISO stakeholders under its shared governance process and the NYISO Independent Board of Directors. Notably, the Commission and other state policymakers have not yet signed on to this proposal and NYISO has publicly stated that it will not move forward until that agreement is in place.

Once approval at the state level has been secured, the NYISO then would submit a filing to FERC to revise NYISO's governing documents to implement the carbon price proposal and ask FERC to approve those revisions as "just and reasonable" under Section 205 of the Federal Power Act.

In light of those significant regulatory hurdles, NYISO states that the carbon pricing would not be implemented in its wholesale markets until the second quarter of 2021, at the absolute earliest.

4. Effect on Retail Compensation

Though not the subject of the ACE-NY report, implementation of a carbon price in the wholesale markets will impact the retail markets as well. Distributed energy resources, such as residential and commercial-scale solar and energy storage projects, typically receive compensation through the VDER value stack or through a net-metering tariff.

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Absent regulatory adjustments, the NYISO carbon price likely would increase VDER compensation for existing and new distributed solar and/or storage projects. The “energy value” in the VDER value stack is variable and directly based on NYISO’s Day-Ahead Energy Market prices. Accordingly, to the extent a carbon price increases those wholesale market energy prices, VDER’s “energy value” will likewise increase. By the same token, a rise in NYISO’s capacity market prices would likely mean a corresponding rise in VDER’s “capacity value.” Though the carbon pricing proposal only would apply to wholesale energy markets, NYISO has found that it could have an impact on capacity markets as well and that methodology adjustments “will be evaluated and discussed” through existing NYISO processes. Finally, implementation of a carbon price likely will precipitate a reevaluation of VDER’s “environmental value.” Policymakers will need to consider whether the “environmental value” is duplicative of a carbon price or instead represents the avoided environmental cost of non-carbon pollution, including local pollutants such as nitrogen oxide, sulfur oxide, and particulate matter.

For retail net-metered projects, any compensation change due to a carbon price would depend on how load serving entities refund the amounts collected from emitting generators to their end-users. If the funds are used to offset increased electricity prices for customers and \$/kWh retail rates stay roughly the same, there should be minimal impact on net-metered compensation.

To learn more about the NYISO carbon pricing initiative and how it would affect your business, please contact a member of Hodgson Russ’s Renewable Energy Practice at <https://www.hodgsonruss.com/practices-renewable-energy.html>.

If you received this alert from a third party or from visiting our website, and would like to be added to our Renewable Energy mailing list, or any other mailing list, please visit us at: <https://contact.hodgsonruss.net/signup/BrandedFormNew.aspx>.

[1] <https://www.nyiso.com/documents/20142/3036629/Locational%20Based%20Marginal%20Pricing.pdf/4d9d692b-6fc3-88a9-ba31-5353786d4c58>

[2] NYISO Proposal, at 8.