



May 2017

At a Crossroad, FERC Conference Addresses State Actions in the Context of Federal Wholesale Market Integrity and Potential Paths Forward

On May 1 and 2, 2017, representatives from northeastern states, wholesale markets, electric utilities, independent power suppliers, and advocacy groups participated in a two-day technical conference at the Federal Energy Regulatory Commission (FERC) to discuss the long-term future of and interaction between FERC-regulated wholesale markets and state energy policies. The conference addressed the development of regional solutions to reconcile the competitive wholesale market framework with increasingly active state participation in supporting particular types of electric generation resources, such as Renewable Portfolio Standards (RPS) and payments for renewable and nuclear energy for their environmental attributes. Discussions focused on whether FERC should “accommodate” state actions, help to “achieve” state goals, or simply let interested parties continue to litigate these issues and accept the results. However, the “elephant in the room” was left mostly unaddressed, at least explicitly: if, and the extent to which, state actions directly affect or interfere with wholesale power markets and thus, under 2016 U.S. Supreme Court decisions,¹ are preempted by FERC’s authority under the Federal Power Act.

The conference sought to address solutions to state actions and preferences that, according to some participants, distort the results of wholesale energy markets, especially in the capacity and procurement areas. As states continue to provide mandates and credits to certain generation technologies, these actions can distort the pricing of wholesale capacity markets, which are designed to ensure sufficient present and future generation exists to meet electric demand reliably and efficiently. FERC-regulated wholesale markets currently can utilize a “minimum offer price rule” (MOPR) to mitigate the impacts of these preferences.

¹ See *Hughes v. Talen Energy Marketing*, No. 14-614, 578 U.S. ___ (2016) (holding that state resource procurement was pre-empted by FERC’s jurisdiction); *FERC v. Electric Power Supply Assn.*, No. 14-480, 577 U.S. ___ (2016) (holding that FERC’s regulation of demand response was jurisdictional and not arbitrary or capricious). See also *Oneok v. Learjet*, 135 S.Ct. 1591 (2015) (emphasizing the importance of considering “the target at which the state law aims” in determining whether state law is preempted).

Day One: Regional Discussions and Urgency

At the outset of the conference, FERC Acting Chairman Cheryl LaFleur stated that “we must shape options and recommendations for a ‘FERC 2.0’” following the restoration of a quorum at the Commission. LaFleur also emphasized that the attendees had “a moment in time” to confront these increasingly urgent issues, despite the present lack of quorum. The first day of the conference addressed the three organized markets individually: ISO New England (ISO-NE), New York Independent System Operator (NYISO), and PJM Interconnection (PJM).

- > In ISO-NE, certain state representatives worried that strong state actions, given the current state of wholesale markets, would result in a “train wreck” leading to the unwinding of capacity markets. Certain state representatives recommended that the industry “marry” wholesale markets with state interests, but expressed reluctance to accept intervention from the wholesale markets and FERC. Market and industry interests took a different view, contending that FERC and the wholesale markets should play a significant role in ensuring resource adequacy and just and reasonable electric rates. Certain of these participants also expressed concern regarding the continuing reliance on gas-fired generation in a constrained market due to a lack of sufficient pipeline capacity. The natural gas industry was not represented at the conference, with the exception of certain generators (who also have other “non-gas” types of generation in their portfolio).
- > In NYISO, New York State and City representatives stressed the urgency of the issues before them, and called for FERC to seek to “harmonize” its efforts with evolving state policy goals for a 21st century electric system. Some industry and market representatives took a longer view – referring to state de-carbonization and renewable goals as a “marathon,” but looking to the wholesale market and FERC to provide clear signals to the industry that preserve the integrity of wholesale power markets and incentivize investment.
- > In PJM, much of the discussion focused on state credits granted to both renewable and zero-emissions facilities such as nuclear generation. State and government representatives reiterated both the importance of resource adequacy and the support of nuclear generation, but contended that the issues faced by PJM are currently less dire than those in New England or New York. State representatives also noted that “markets are not sacrosanct” but instead exist to serve state purposes, and expressed concern over the market’s heavy reliance on natural gas generation. Certain industry and market representatives expressed concern regarding state actions, fearing that they could be “contagious” with several participants advocating for strong protections and market corrections (such as the MOPR) to ensure a well-functioning wholesale market.

Day Two: Potential Solutions and Paths Forward

The second day of the conference reviewed the implications of state policies across all three regions, and then invited industry experts to discuss the potential solutions that would preserve the benefits of wholesale markets while respecting state policies.

- > In his initial remarks, J. Arnold Quinn (the moderator of the technical conference and the director of FERC’s Office of Energy Policy and Innovation) set out five “paths forward” that had become apparent from the feedback provided during the previous day’s panels: (1) limited to no interference from FERC, (2) deference from FERC to the states, but FERC would take action to ensure accurate capacity prices (also known as “accommodation”); (3) resolution via litigation; (4) using the wholesale markets to “achieve” state policy goals, such as through a carbon price, or (5) an extremely strong MOPR that would mean that if a resource received state support, that resource would not clear in the capacity markets and thus would not receive capacity payments. Discussion focused on two of these paths: Path 2, the “accommodation” path, and Path 4, the “achievement” path.
- > The representatives of private interests, including major utilities and independent power producers, appeared to welcome the prospect of wholesale market carbon pricing as an alternative to the “mandate-driven world” of state policies. Multiple industry participants expressed concern that too much “accommodation” of state interests could be irreparably harmful to the integrity of wholesale markets. Certain state representatives remained leery of what they viewed as federal interference with state action

and expressed a preference that their policies be “accommodated,” rather than “achieved,” by FERC and the wholesale markets. New York took a stronger stance, asserting FERC must “harmonize” its efforts with State policy.

- > Finally, a panel of subject-matter experts generally echoed the need for protection of wholesale markets, and for markets to be designed to account for state policies. The panel also discussed the potential for wholesale markets to price carbon. Among other things, Dr. William Hogan, the Research Director of the Harvard Electricity Policy Group, jokingly called for the implementation of a “carbon banana”: pricing carbon in the electricity markets but avoiding calling such a practice a carbon tax. The panelists universally supported the benefits of wholesale markets’ ability to meet policy goals efficiently, and asked FERC to make “hard decisions” to support the ongoing development and viability of wholesale markets.

In the closing of the conference, Acting Chairman LaFleur and Commissioner Colette Honorable both delivered closing remarks. Commissioner Honorable (who has announced that she will not seek another term at the Commission) agreed that FERC needed to support the “core principles of markets,” and demonstrate “political courage” going forward, while calling for comments following the conference regarding the “accommodate” and “achieve” paths. Acting Chairman LaFleur addressed each region in turn, noting that ISO-NE was the “farthest along” of the three regions while NYISO was in a “preliminary” stage, but she expressed confidence that “a one-state ISO and a state can work out policy.” For PJM, she stated that the more difficult “achieve” path was “more likely to result in an actual resolution.” Generally, and longer-term, she believed that the conference sent “a clear message that we have to look beyond the capacity markets,” and that current market structures may need significant reform.

Going forward, the issues discussed at the technical conference will be addressed in a number of different proceedings, which could change depending on which of the five paths forward FERC chooses. As of now, the issues will be addressed in the following proceedings:

- > First, parties were invited to file comments in the technical conference docket. The official announcement requesting such comment has not yet been issued.
- > Second, multiple matters relating to these issues are presently before the Commission:
 - > For ISO-NE, Docket Nos.:
 - > ER13-2266-000 *et al.*, addressing the ISO-NE Winter Reliability Program and
 - > ER17-795, addressing adjustments to Cost of New Entry and MOPR values for ISO-NE’s Forward Capacity Market.
 - > For NYISO, Docket Nos.:
 - > ER16-1404, addressing the development of the renewables exception to NYISO’s MOPR;
 - > EL13-62, addressing the development of mitigation measures to address the impact of reliability-must-run (RMR) units on NYISO capacity markets;
 - > EL16-92-001, addressing the exemption of NYISO demand response participants from NYISO MOPR, and
 - > EL15-37 and ER16-120, addressing NYISO tariff revisions for RMR units.
 - > For PJM, Docket Nos.:
 - > EL16-49, addressing a complaint regarding Illinois Zero-Emission Credit legislation;
 - > EL14-48, ER14-1461, EL15-29 and ER15-623, addressing tariff revisions to PJM’s capacity market, and
 - > ER17-367, addressing aggregation and seasonal distinctions in PJM’s capacity market.
- > Third, each of the three RTO/ISOs are developing solutions via their internal stakeholder processes, such as NEPOOL’s Integrating Markets and Public Policy (IMAPP) process for ISO-NE and the Integrating Public Policy initiative for NYISO. At the conference, representatives from PJM indicated that their own stakeholder process would begin shortly.

- > Fourth, two important lawsuits are currently pending in Illinois and New York federal courts regarding the payment of credits to non-emitting nuclear facilities designed to provide value for their carbon-free emissions.²
- > Finally, it is also possible that FERC, after the restoration of a quorum at “FERC 2.0,” will initiate a rulemaking proceeding to address the issues arising out of this technical conference.

LaFleur suggested that FERC may need to take action in a number of proceedings to address these issues. Whichever path or paths FERC ultimately chooses, the outcome of the issues addressed by this conference and future proceedings will shape the landscape of FERC-regulated wholesale markets for years to come.

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² See *Electric Power Supply Assoc. et al. v. Star et al.*, case no. 1:17-cv-01164 (N.D. Ill. 2017) and *Coalition for Competitive Electricity et al. v. Zibelman et al.*, case no. 1:16-cv-08164 (S.D.N.Y. 2016).

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