Comments on Greenhouse Gas Coordination

Working Group Meeting – January 21, 2025

Department of Market Monitoring

February 11, 2025

Summary

The Department of Market Monitoring (DMM) appreciates the opportunity to comment on the California ISO's *Greenhouse Gas Coordination Working Group* meeting held on January 21, 2025.¹ The presentation addressed two topics: (1) the further specification of the accounting and reporting approach to allocating greenhouse gas (GHG) emissions to entities not in priced GHG regulation areas and (2) the no GHG cost reference pass counterfactual. DMM offers brief comments on each of these topics below.

DMM continues to support development of the accounting and reporting approach

DMM continues to support the further development of the accounting and reporting approach as a near-term means of incorporating non-priced GHG policies into the extended day-ahead market (EDAM). The accounting and reporting approach is a wholly out-of-market approach that leverages and enhances existing market processes and data to allocate GHG emissions to entities in areas with non-priced GHG policies. The primary benefit of this approach is that it is a non-market process that attributes GHG emissions after the market runs, and as such would likely have minimal direct market impacts.

The counterfactual method with no GHG cost may minimize the likelihood of secondary dispatch, but introduces additional complexities to the overall market design

The discussion of the counterfactual reference pass with no GHG costs focused on examples designed to demonstrate how the no GHG cost reference pass counterfactual would work, and why it could lead to the over-collection of GHG revenues. The ISO also discussed potential approaches to address the over-collection of GHG revenues under the no GHG cost counterfactual method.

The no GHG cost counterfactual method sets the baseline reference by calculating the optimal dispatch for the whole EDAM footprint, excluding GHG costs. The baseline is then used to identify which imports into priced GHG regulation areas would be due to the inclusion of GHG costs into the market optimization. This approach is distinct from the method currently approved for use in EDAM (CAISO method) and the method proposed by Vistra and other stakeholders (Vistra et al method) because it does not limit the optimized counterfactual dispatch to either the non-GHG regulation areas or individual non-GHG regulation balancing areas.

One of the potential advantages of this approach is that this counterfactual takes into account the entire EDAM grid area and all potential transfers and resources, which leads to a more complete accounting of transmission constraints and resulting congestion. Additionally, the use of the whole EDAM area in the

¹ GHG Coordination Working Group - January 21, 2025, California ISO, January 21, 2025: <u>https://stakeholdercenter.caiso.com/StakeholderInitiatives/Greenhouse-gas-coordination-working-group</u>

reference pass results in a counterfactual with full economic displacement across all EDAM BAAs. This may reduce the likelihood of estimated secondary dispatch because the pool of attributable resources will be smaller due to the allowance for transfers into the priced GHG regulation areas.

In the working group presentation, the ISO further elaborated on the potential for over-collection of GHG revenues in the no GHG cost counterfactual method. The potential for over-collection of GHG revenues arises from the fact that all imports into a GHG regulation area are settled on the marginal price, which includes the GHG marginal cost component, but only attributed imports are paid the GHG marginal cost component. In the case of the CAISO method and Vistra et al methods, this is not an issue because those reference pass counterfactual methods do not include imports into priced GHG regulation areas, and as such all imports into those areas are attributed.

However, in the case of the no GHG cost counterfactual method, there may be a mix of imports that are attributed and unattributed. This is because the no GHG cost method optimizes across the entire EDAM footprint and permits imports into GHG regulation areas in the reference pass. These imports into GHG regulation areas that occur in the reference pass are not attributed, and as such are not paid the GHG marginal cost component. This can lead to over-collection of GHG revenues.

The ISO put forward two possible remedies for over-collection. The first proposed remedy was an uplift payment to load, equivalent to the charged GHG cost for unattributed transfers. The second remedy recognizes that unattributed transfers into a GHG regulation area carry a cost that priced GHG regulation areas wish to capture. To capture that cost, the ISO proposed calculating the average GHG cost of unattributed reference imports into priced GHG regulation areas. That average cost would then be used to calculate the total GHG cost of those unattributed imports, subtracted from the over-collected revenue, and given to the relevant regulatory agencies. The remaining portion of the over-collected revenue would be returned to load.

The second remedy described above requires that the ISO develop a means of calculating the cost of GHG associated with non-attributed imports into priced GHG regulation areas. The introduction of a non-marginal pricing approach to GHG, and an uplift payment into the settlement process for GHG costs, would introduce additional complexities into the overall market design. As such, the ISO should specify in greater detail how the pricing mechanism, settlement, and uplift payments would be determined, in order to allow more complete analysis of this proposed approach.

The no GHG cost counterfactual approach does not account for implicit GHG costs included in energy bids of resources in priced GHG regulation areas

DMM recognizes that the no GHG cost counterfactual is a new possible approach that is still under development. As noted in previous comments, one important element missing from the proposed no cost GHG counterfactual is an approach to extract or control for the GHG costs in priced GHG regulation areas.² For resources within priced GHG regulation areas, GHG costs are implicitly included in the energy bids rather than explicitly included as a discrete component of the bids. This is in contrast to resources in non-priced GHG regulation areas, which include an explicit and discrete GHG bid cost adder.

² Comments on Greenhouse Gas Coordination 11-12-2024 Working Group Meeting, Department of Market Monitoring, November 26, 2024: <u>https://stakeholdercenter.caiso.com/Common/DownloadFile/64a1c706-1b28-44fd-88a2-5a46175ec1dc</u>

If the embedded GHG costs are not extracted from the bids of resources in priced GHG regulation areas, the no GHG cost counterfactual method would not provide an accurate measure of what the optimal solution would have been in absence of any GHG costs in the market footprint. DMM requests that the ISO propose one or more methods for how this could be achieved.