




Friday, September 03, 2010 2:49 PM ET  **Exclusive**

Despite death of S.B. 722, California TRECs markets seen forging on

By Amanda Luhavalja

As the final hours of the 2010 legislative session wound to a close in California on Aug. 31, a bid to adopt an amended S.B. 722, which would have put into law a 33% renewable portfolio standard by 2020, fell by the wayside before it could be approved by the state Senate.

As the clock ran out, sources said, S.B. 722 ultimately remained bogged down by many of the same issues that dogged the bill in the first place, including the importation of out-of-state power and provisions that restrict the procurement target to no more than 10% of out-of-state renewable energy credits.

"As CA Legislature failed to pass a renewable power bill, CA's new governor will decide the fate of the state's proposed 33% renewable power mandate by 2020 as well as any restrictions to meet the state's renewable mandate with out-of-state resources," said an analyst note from Macquarie released Sept. 1. "While CA utility regulators have proposed to address the latter issues and the California Air Resources Board should implement the 33% mandate through executive decisions, they can be easily revoked by the new governor, we understand."

While the ongoing regulatory uncertainty in California has paralyzed the Western market for trading RECs thus far, according to some market insiders, the latest development on the legislative front does provide some needed clarity for market participants.

California is, in fact, moving ahead with the development of its RPS, said a renewable energy policy analyst for the Database of State Incentives for Renewable Energy.

Anticipating such a legislative deadlock, the California Public Utilities Commission released a proposed decision Aug. 25 that would allow investor-owned utilities to use tradable renewable energy credits, or TRECs, to meet up to 40% of their annual renewable power procurement mandates.

"With the death of this bill, attention now turns to the CPUC who is charged with interpreting and enforcing the existing RPS. In advance of yesterday's SB 722 deadline, the CPUC issued a proposed decision which provides insight on how the commission will interpret the CA RPS in the absence of legislative guidance (SB 722)," John Friskel, Western Electricity Coordinating Council broker with Clear Energy Brokerage & Consulting LLC, said in an analyst note Sept. 1.

The proposed decision, written by commission President Michael Peevey, would broaden the utilities' access to TRECs and allow some energy deliveries made under existing contracts to avoid being categorized as TRECs. The decision would not, however, expand the criteria to determine what types of energy transactions result in TRECs.

"The CPUC proposed decision is friendlier to utilities and out of state generators as it provides additional RPS flexibility," Friskel wrote.

According to the CPUC Aug. 25 draft, allowing the use of TRECs for RPS compliance would give RPS-obligated retail sellers increased options for RPS compliance and may reduce complexity in RPS procurement contracting.

The PUC on March 11 unanimously authorized the procurement and use of TRECs for compliance with the renewable portfolio standard. However, on May 6, the PUC voted to stay its March decision after California's investor-owned utilities, independent power producers and marketers called on the state's utility regulators to rethink the decision, saying it will discourage renewable energy development throughout the West and has already created uncertainty for all market participants.

Among other things, the petitioners asked for fewer restrictions on qualifying TRECs for RPS compliance, asking that a 25% cap be removed from the amount of TRECs that can be used for RPS compliance rather than so-called bundled transactions, in which the output from specified renewable energy projects is delivered to California instead of being credited through transactions that allow utilities to buy the green attributes after the power was generated.

A TREC represents proof that 1 MWh was generated from an eligible renewable energy resource and can be traded and sold independently of the energy it represents anytime before its three-year expiration date. Utilities would have flexibility, such as being able to buy TRECs representing energy sold outside the state from California generators, in meeting the RPS, which now calls for 20% of each utility's retail electricity sales to be generated by renewable energy sources.

Because the state's retail electric service providers have had to buy energy and RECs together under bundled contracts, in March, Peevey said this had resulted in inefficiency because California did not have a secondary market where RECs alone could be traded. Wholesale purchasers of renewable energy could not market any renewable energy they bought in excess of RPS compliance, he said.

In some instances, renewable energy developers might want to separately sell RECs and energy to command the most value, Peevey said. "I believe a more liquid RECs market and forward price curve will stimulate renewable energy development," he continued.

Friskel told SNL Energy on Aug. 31 that the ongoing TREC debate had been "holding up a lot of sellers, who are overly optimistic in a market that is both oversupplied and filled with uncertainty."

"Although the CPUC has proposed increasing the TREC to 40%, the [California Energy Commission] TREC market is still oversupplied. This would indicate downward pricing pressure. Countervailing this downward pressure, utilities are keen to take full advantage of TREC purchasing because it is typically the least cost path to compliance," Friskel wrote. "Furthermore, conservative utilities want to procure for compliance quickly. Clear Energy believes the price target of \$15-\$25 is aggressive but obtainable in the early stages of CA TREC trading. Expect to see prices erode as utilities approach their TREC limit."

Friskel wrote: "For CEC REC owners, it is Clear Energy's view that the defeat of SB 722 and the CPUC's proposed decision benefits CEC certified REC owners in several ways. Firstly, SB 722 would have handcuffed the CPUC's ability to employ TRECs as a compliance instrument. It restricted the limits of REC trading to 10%, and it was questionable to what extent the CPUC had authority to adjust the language written into the bill. Now, as before, the CPUC has the authority to increase the TREC trading limits to the benefit of California ratepayers and CEC REC holders."

While the CPUC decision is still a moving target, he said, the failure of S.B. 722 does provide a "level of regulatory clarity in an opaque market." Clear Energy expects increased market liquidity in the coming months, Friskel told SNL.

<http://www1.snl.com>