House Passes Combined Renewable Electricity/Energy Efficiency Standard

July 8, 2009

ENERGY TECHNOLOGY & RENEWABLES ALERT - JULY 8, 2009

written by Eric W. Macaux, Mark A. Barnett, Mary Beth Gentleman

On June 26, 2009, the U.S. House of Representatives voted 219-212 to pass the American Clean Energy Security Act (the "House Bill") [.pdf], which included a national combined renewable electricity/energy efficiency standard ("RES"). Currently, twenty-nine states and the District of Columbia have in place some form of renewable energy portfolio standard [.ppt], but the adoption of a federal RES is widely thought to be important for the creation of a national renewable energy and energy efficiency market. The RES passed by the House would not preempt state programs with stricter compliance targets, meaning that the federal program would preserve to some extent the patchwork of state standards. The interaction between state programs and a federal RES may be particularly important where there are significant differences with respect to what generation technologies qualify and whether or how electricity savings may be used to meet compliance goals. Although the final contours of the RES will remain uncertain until it is enacted, the degree of federal preemption will be a key issue for states with aggressive clean energy agendas.

How the RES Works

The House RES establishes a national compliance obligation overseen by the Federal Energy Regulatory Commission ("FERC") under which large (4 million MWh of retail sales and larger) retail electricity suppliers ("Suppliers") are required to invest in renewable energy and energy efficiency. For each compliance year, a Supplier must calculate its total volume of electricity sales during that year (the "base amount") and then submit to FERC a sufficient number of federal renewable electricity credits ("Federal RECs") and demonstrated annual electricity savings to meet the RES goal for that compliance year. Excess Federal RECs may be banked for as long as three years.

Combining energy efficiency and renewable energy under a single standard is thought by the bill's proponents to reduce the cost impacts associated with moving the nation away from fossil fuel-based generation to meet load requirements. As adopted by the House, up to 25 percent (or 40 percent, upon a state's request) of a Supplier's RES obligation may be met through electricity savings rather than Federal RECs. The trade-off, however, is that the incentive to develop and deploy new renewable energy capacity may be diluted by allowing Suppliers to meet up to 40 percent of the standard through efficiency measures.

The House Bill creates an escalating RES goal that begins in 2012 and increases every two years until 2020. Compared to Massachusetts' renewable portfolio standard [.pdf] for Class I renewable resources as amended last year, the House RES

obligation is weaker in its early years but rises quickly to become more rigorous. The final goal, 20% by 2020, is substantially higher than Massachusetts' goal of 15% and is more aggressive than nearly any other New England state. By comparison, the RES currently being considered in the Senate [.pdf] starts out lower than both the House RES and Massachusetts' program (3%), and it remains so, reaching 15% in 2021.

Compliance Year	Federal RES (%)	Senate RES (%)	Massachusetts (%)
2009	--	--	4.0
2010	--	--	5.0
2011	--	3.0	6.0
2012	6.0	3.0	7.0
2013	6.0	3.0	8.0
2014	9.5	6.0	9.0
2015	9.5	6.0	10.0
2016	13.0	6.0	11.0
2017	13.0	9.0	12.0
2018	16.5	9.0	13.0
2019	16.5	12.0	14.0
2020	20.0	12.0	15.0
2021-2039	20.0	15.0	Increases 1% annually

The comparison suggests how important federal preemption may be for businesses in the energy space. Not only does Massachusetts' program differ from the House and Senate RES programs with respect to its annual compliance obligation, Massachusetts is also among those states that do not allow electricity savings to be applied toward the target percentage. Thus, having a clear understanding of how various states' programs overlap with and differ from a federal RES will be important for businesses looking for competitive advantages.

Meeting the RES Goal: Renewable Electricity

Like most state programs, the House RES would allow qualified generators to earn one Federal REC for each megawatt-hour of renewable electricity produced. However, "renewable electricity" is defined broadly and includes electricity generated from (1) renewable facilities as well as from (2) other qualifying energy resources. The list of eligible renewable resources closely resembles the technologies that may qualify as "renewable" under most state renewable energy programs and under the federal tax code: wind, solar, geothermal, biomass, biogas, biofuels, hydrokinetic, and some hydropower. The second category of "other" resources includes technologies that, while not "renewable", may be cleaner sources of electricity than most fossil fuels. The technologies in this category are landfill gas, wastewater treatment gas,

waste-to-energy, and coal mine methane. While critics have urged that inclusion of non-renewable resources under a federal RES will dilute the program's environmental benefits, the narrow 7-vote margin in the House indicates that such compromises may be necessary for the RES to become law.

Suppliers operating in states that have adopted a renewable energy standard may apply any payments made toward compliance with such standard toward the RES, including the purchase of state-issued RECs and alternative compliance payments. Thus, the RES as enacted by the House does not directly supersede state requirements. Suppliers will still want to track closely the source of the RECs they purchase. Unlike many states' programs, the House RES includes a 3x multiplier for renewable energy generated by "distributed resources", making RECs from those sources a particularly valuable commodity. "Distributed Resources" are defined as those that primarily serve electricity users at or near the facility site and whose capacity is no greater than 4 MW (2 MW for existing resources). The rules applicable to distributed resources are complex, however, and differ for new and existing facilities. A close read of these sections is warranted for businesses wishing to leverage potential business opportunities.

Meeting the RES Goal: Electricity Savings

Under the House bill, FERC has been tasked with regulating how "electricity savings" can qualify for RES compliance purposes. "Electricity savings" includes reductions in electricity use achieved through customer-side energy efficiency, reduced line losses, increased combined-heat-and-power efficiency, and the use of new or more efficient fuel cells. FERC would be responsible for issuing protocols and standards addressing at least thirteen issues related to determining what "electricity savings" can be counted towards the RES.

Meeting the RES Goal: Alternative Compliance Payments

Where a Supplier has not obtained a sufficient number of Federal RECs or demonstrated electricity savings to meet the RES goal, it may make an alternative compliance payment ("ACP") of $25 per MWh. This is lower than the ACP of many states that have been investing heavily in renewable energy, including Massachusetts ($60.92/MWh) and New Jersey ($50/MWh), suggesting that the trading price of Federal RECs will be lower than those states' RECs.

Federal ACP payments are made directly to the states in which a Supplier operates in proportion to the retail sales attributable to that state. The receiving state may use ACP funds to promote the deployment of renewable energy resources or the implementation of energy efficiency measures.

What Comes Next

Passage of the House Bill is undoubtedly significant, but it remains unclear how that will compare with the Senate's energy bill, which has been reported out of committee but not formally introduced. Although the text of the Senate's draft is not yet

released, early reports show a combined efficiency-renewables RES that resembles – at least structurally – the House version. However, as noted above, there appear to be significant differences between the House and Senate with respect to how aggressive the RES targets should be. Given the narrow margin by which the House bill passed and the reluctance of coal-state Democrats in both the House and Senate to support a high RES goal, it is unlikely that the Senate's RES target would increase as a result of further committee and floor debate. If Congress does pass a federal RES, leveraging the resulting business opportunities will thus require an intimate understanding of how both federal and state programs work and, perhaps more importantly, how they interact.