

Market prepares for both carbon and REC markets

Washington DC—Published: 23 Feb 2009 14:40 EST

Market participants are bracing for overlapping US carbon and renewable energy legislation.

According to timelines laid out by some US lawmakers, a law setting a federal renewable portfolio standard (RPS) is likely to be passed before a climate change bill this year, creating a national market for renewable energy credits (RECs) before a federal carbon cap-and-trade system.

A federal RPS would have major implications for the emergence of a US carbon market because more aggressive production of emission-free renewable energy would contribute to the reductions aimed for in a carbon cap-and-trade system.

The Senate and House of Representatives will take up energy legislation, which will include creating a national RPS, in the next few weeks, Senate Leader Harry Reid and House Speaker Nancy Pelosi have said today at a Washington energy event.

Senator Jeff Bingaman, the Democratic chair of the Senate energy committee, will take the lead on drafting a national RPS bill this spring which would require 20 per cent of electricity sold in the US to come from renewable energy.

Congressman Ed Markey, chairman of the air quality subcommittee of the House of Representatives energy and commerce committee, has already introduced a bill requiring one-quarter of electricity sold in the US to come from renewables by 2025.

Clarity

But market participants hope Congress will clearly spell out what constitutes a REC - a credit for a MWh of renewable energy produced - and how it will differ from CO2 emission allowances or emission-reduction credits before the two markets run in parallel.

"I think the regulators have to decide is there some cross over point between the both markets," said Peter Zaborowsky, managing director of environmental markets at Evolution Brokers.

"Renewable generators create valid carbon reductions but sometimes not directly," Zaborowsky said. "You have to make sure whether you are double counting for (those) reductions."

RPS goal

With a national REC market set to precede a national carbon market, some of the potential overlap can be clarified by clearly stating the aim of the RPS.

"The main issue at hand is whether or not one of the goals of the RPS policy is to reduce greenhouse gas emissions," said Jennifer Martin, deputy director at San Francisco-based Center for Resource Solutions.

According to Martin, most RPSs have a number of goals, from increasing energy security to creating green jobs.

But if one of the stated goals of the programme is to reduce GHG emissions, measures should be taken to address how the reduction would be addressed in the carbon and REC markets and that renewable energy generators are rewarded for the CO₂ benefits of the power they produce.

"If GHG benefits is stated as one of the goals - and carbon policy comes in - you need to make sure that the way that allowances are assigned or allocated ... maintain the benefits of the RPS policy," she said.

Renewable energy's CO₂ reduction ability could be left out "unless explicitly accounted for," her organisation contends.

Cap-and-trade programme set-asides, like in the northeastern states of the Regional Greenhouse Gas Initiative (RGGI) - a mandatory carbon cap-and-trade system - "allow REC marketers to make legitimate carbon reduction claims on RECs generated in the region," she added.

State example

Adam Raphaely, an environmental markets broker at TFS Energy, said lawmakers should look to states such as those in RGGI that have experience with compliance REC and carbon markets for guidance.

"With both of them (the REC and carbon markets) going towards compliance, I think that we can look to existing compliance markets where they are running successfully in parallel with one another," Raphaely told Point Carbon.

Nine of the 10 states that participate RGGI also have a RPS in place.

In RGGI, states have set aside a small percentage of allowances that would have otherwise been auctioned to emitters and retire them to account for the emissions avoided through the use of renewable energy embodied by RECs.

The set-aside enables those marketers to claim that the electricity they sell in a carbon capped region also accounts for a reduction of greenhouse gas emissions and causes the cap to be tightened.

Going national

Nearly 30 US states have in place some form of RPS with varying degrees of stringency and differing definitions of what constitutes renewable energy.

Establishing a mandatory RPS for all 50 US states and a national REC market would be relatively easy and quick to set up, said Evolution's Zaborowsky.

He explained that more than half of the states have set up renewable energy tracking systems within their regional transmission systems.

"You already kind of have some critical mass in the system. To extend that on a nationwide basis - once you have a tracking system so these RECs can be minted...it should be pretty easy to move to a functioning national market," he said.

Faster than carbon market

A national REC market could also be established much faster than a domestic greenhouse gas emissions trading system, said Randall Lack, managing director for Element Markets.

Lack anticipates that the US will have carbon cap-and-trade legislation done by 2010 or 2011.

"Then it will take at least two years to figure out the regulation. You are still going to have litigation over allowance distribution and there is still going to be some fighting about what it's going to look like," Lack said.

Meanwhile, once a federal RPS bill is passed, a fully functioning market could take off relatively soon thereafter.

"The market can respond quicker to that and a lot of the major utilities already have REC positions and experience," he added.

Lack sees a carbon market in the US being "clearly separate and distinct" from the national REC market that emerges.

"Although there will be some interplays for project developers as the GHG market will increase the demand for renewables and the GHG price will be factored into the power price, so renewables will be winners on multiple fronts," Lack said.

By Valerie Volcovici — vv@pointcarbon.com