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Client Alert

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If you read one thing...

- The California Legislature has approved an ambitious plan to boost targets for renewable energy generation and energy efficiency but has rejected proposals to reduce petroleum usage by 50 percent and to reduce California's greenhouse gas (GHG) emissions by 80 percent by 2050.
- Awaiting Gov. Brown's signature, SB 350 contains important changes for both utilities and renewable energy developers with regard to renewable energy credit banking and compliance, Power Purchase Agreement (PPA) contract durations and regional energy markets under California's Renewables Portfolio Standard (RPS).

California Legislature Boosts Renewables Portfolio Standard to 50 Percent and Increases Energy Efficiency Goals; Balks at Increased Reductions in Greenhouse Gas Emissions and Petroleum Use

Following a raucous debate fueled by intense lobbying by environmental organizations and the oil industry, the California Legislature has approved an ambitious plan by Gov. Jerry Brown (D) to boost targets for renewable energy generation to 50 percent and to increase energy efficiency. However, the Legislature rejected proposals to reduce petroleum usage by 50 percent and to reduce California's GHG emissions by 80 percent by 2050.

Long at the forefront of public policy to combat climate change and develop renewable energy, California adopted the nation's first RPS for investor-owned utilities in 2003 and, in 2006, launched an ambitious program to reduce GHG emissions by 20 percent below 1990 levels by 2020. California has developed a Low Carbon Fuels Standard to reduce the carbon intensity of transportation fuels and has derived more than $2 billion by selling credits through its cap and trade program to reduce GHG emissions.

Seeking to build on these successes and burnish his legacy, Gov. Brown used his January inaugural address to call for increasing the target for California's RPS from its current 33 percent to 50 percent by 2030, doubling energy efficiency targets for public and private buildings, and reducing petroleum consumption in transportation by 2030. Senate President Pro Tempore Kevin De Leon (D-Los Angeles) introduced legislation (SB 350) to codify Gov. Brown's goals. Legislators also introduced a dozen separate measures to address climate change, including SB 32, that would have required California to reduce emissions 80 percent below 1990 levels by 2050.

Passed in both the California Senate and the Assembly and now awaiting Gov. Brown's signature, SB 350, The Clean Energy and Pollution Reduction Act of 2015, contains important changes for both utilities and renewable energy developers:

- **RPS**. Increases, from 33 percent to 50 percent, the California RPS target for electricity procured from eligible renewable energy resources for both investor- and publicly-owned utilities. Utilities would be required to procure 40 percent of their retail sales from renewable resources by the end of 2024, 45 percent by 2027 and 50 percent by 2030.
- **PPA contract duration**. Requires that at least 65 percent of RPS procurement come from either power purchase contracts of 10 years or greater duration or from utility ownership of eligible energy resources beginning in 2021. (Note: This is a key provision in the expanded RPS and a hard-fought win for the utilities. Starting in 2021, utilities can insist that much of the growth in the renewable energy obligations that they are purchasing be on short-term contracts. This could create significant problems for renewable developers seeking to finance their projects with long-term debt.)
- **Banking and compliance**. Allows unlimited banking of so-called "Bucket 1" renewable energy resources, regardless of contract length, beginning in 2021. This provision allows utilities that procure renewable power in excess of a statutory RPS target for a compliance period to bank that excess power to count toward RPS compliance in a future period. "Bucket 1" refers to the requirement in California law that utilities procure a majority of renewable power from eligible resources that tie into a balancing authority located in-state.
- **Rooftop solar**. Prohibits renewable energy credits associated with electricity sold to utilities through net metering by a customer to be counted toward utility RPS procurement compliance.
- **Regional energy market**. Declares the intent of the Legislature to transform the California Independent System Operator ("CAISO") into a regional organization to promote electricity markets in the western United States and establishes a process for CAISO to change its bylaws and governance subject to approval by the Legislature.
- **Energy efficiency**. SB 350 also sets more ambitious goals for increasing energy efficiency in public and private buildings by 50 percent by 2050 and directs the California Energy Commission (CEC) and the California Public Utilities Commission (CPUC) to specify programs and funds that will apply toward meeting the goals. The measure places additional emphasis on the role of energy storage and demand response as a way to reduce stress on the electric grid when demand is high and to reward customers for changing behavior in accord with price and demand signals.
- **Transportation electrification**. The measure directs the CPUC to remove regulatory barriers facing utilities in making increased investment in the electrification of the transportation sector. California is focusing on transportation electrification as a key element to reducing both GHG emissions and criteria air pollution in nonattainment areas.

Analysis

While much of the political infighting centered on the increased RPS targets and petroleum reduction proposal, perhaps the most significant changes in SB 350 are the provisions authorizing the transformation of CAISO into a regional energy market. Under SB 350, CAISO would be able to coordinate with other system operators in the West for the generation and transmission of renewable energy across the region. With California utilities currently experiencing overgeneration under California's RPS program, the concept of developing a regional market has garnered support from key stakeholders as a way to both export renewable energy during overgeneration and to provide California utilities with a wider array of options to meet the state's green energy targets more efficiently. Moreover, a regional market could provide additional opportunities for renewable energy developers and generators to sell green power to California from projects located outside the state.

Gov. Brown views developing a regional energy market as a key to boosting renewable energy use in California while keeping costs down. As he recently told the California Chamber of Commerce, "[W]e can't confine ourselves to California. We have to extend to other states. So when the sun is down in one place, we have cheap solar power here and in fact in abundance and we send it to Nevada or Utah or Arizona. And on the other hand, when the sun is higher or the wind is blowing in Wyoming, we can all share that. And with a large region interconnected with a smart grid, you are able to use intermittent power as renewable energy is and you get back a lot of the base load quality that the larger coal and gas plants would provide." SB 350 directs CAISO to work with the CEC and CPUC to develop revised bylaws and other governance documents for legislative approval by the end of 2017.

Not all parties were pleased with the final bill. Rooftop solar developers and utilities were disappointed that SB 350 does not specify that distributed solar arrays count toward the mandatory component of the renewable energy target. The two industries abandoned their push for such a provision in SB 350 in the face of heavy opposition from the Building Trades and other unions and of concerns by some legislators that net metering policies and barriers to expansion of roof top solar in disadvantaged communities amount to a subsidy of wealthier retail customers by the poor.

Environmental groups and Gov. Brown suffered a rare defeat over the SB 350 provision that would have set a target for reducing petroleum use in cars and trucks by 50 percent. The petroleum use reduction proposal was easily the most controversial part of the bill and drew intense opposition from the oil industry and auto manufacturers, who feared that the broad wording of the proposed statute would empower the California Air Resources Board (CARB) to outlaw certain engine classes. Both the oil industry and billionaire activist Tom Steyer spent millions on targeted mail and advertising aimed at persuading legislators to oppose or support the provision. After a block of Democratic legislators balked at supporting the petroleum reduction provisions, the language was stripped out of the bill, clearing the way for its passage.

The fight over the petroleum reduction provisions may not be over. At a press conference called to announce that the provisions would be taken out of the bill, Gov. Brown warned that, "Oil has won the skirmish, but they've lost the bigger battle" and suggested that he may act under his executive authority and existing law to effectuate the reduction targets.

Gov. Brown and his allies were also stung by the defeat of SB 32 (Pavley), a related measure that would have reauthorized California's Global Warming Solutions Act of 2006 beyond 2020 and set higher GHG emission reduction targets. The measure was supported by Gov. Brown and U.S. Sens. Dianne Feinstein (D-CA) and Barbara Boxer (D-CA). The measure drew opposition from a number of Democrats who raised concerns about the broad authority of the CARB to implement climate change policy. Some members proposed to require legislative approval of certain CARB regulations, while others sought to give the Legislature the power to appoint some members of the board. The measure's author, Sen. Fran Pavley (D-Agoura Hills) said that she will bring the bill up for reconsideration early next year. It is unclear whether the measure can gain enough support to pass.

The defeat of SB 32 and the petroleum use reduction provision in SB 350 have raised questions about California's continuing commitment to the climate change leadership mantle. While California is a blue state, where Democrats hold every statewide elective office and large majorities in both houses of the Legislature, a significant number of leaders have raised concerns about the costs of climate change policies to business and poor communities and the broad delegation of authority to the CARB. Yet, it would be an oversimplification to view last week's votes as signaling backtracking in California's direction on energy and climate change. The debate in Sacramento was not about the need for action, but about the pace of change and mitigating collateral impacts on communities of concern. Recent polls show that Californians overwhelmingly support efforts to address climate change, yet they also have concerns about its impact on the cost of energy in their daily lives. Those polls underscore the delicate challenge facing California's leaders as they continue down the path toward a more sustainable energy policy.

Contact Information

If you have any questions regarding this alert, please contact:

Dario J. Frommer
dfrommer@akingump.com
213.254.1270
Los Angeles

George (Chip) Cannon Jr.
ccannon@akingump.com
202.887.4527
Washington, D.C.

Edward W. Zaelke
ezaelke@akingump.com
213.254.1234
Los Angeles