

STATE OF CONNECTICUT
CONNECTICUT ENERGY ADVISORY BOARD

RE: POST-SEMINAR RENEWABLE :
PORTFOLIO STANDARD :
POLICY QUESTIONS : APRIL 21, 2011

**OFFICE OF CONSUMER COUNSEL'S RESPONSES TO
POST-SEMINAR POLICY QUESTIONS POSED**

The Office of Consumer Counsel ("OCC") hereby submits its responses to the questions posed following the April 11, 2011 Seminar.

- 1. What do you see as the primary RPS objectives Connecticut should focus on and commit to over the next 5 to 10 years? In addition, please rank these objectives in order of priority.**

Connecticut should focus on its renewable energy objectives rather than something called "renewable portfolio standard" or "RPS" objectives. RPS requirements are one tool that can be used to reach Connecticut's renewable energy objectives, but they have not proven to be an effective tool for building new, local renewable energy capacity.

Connecticut should decide (i) what premiums, over the projected price of ordinary power, it is willing to pay for new, renewable energy capacity; and then (ii) develop either request for proposal ("RFP") processes or feed-in tariffs that will lead to the "purchase" of such capacity. It is possible that the premiums just mentioned could legitimately be different for different types of renewables. For example, there perhaps could be a different premium for baseload renewables that use fuel (fuel cells, biomass) than for intermittent renewables (wind, solar) that do not use fuel. The size of the premiums is a policy choice that would balance ratepayer costs against the environmental, economic development, and other benefits of renewable energy.

Feed-in tariffs should be used, in OCC's view, only for small projects (perhaps 5 megawatts and under) where the administrative burden of performing active rate

regulation is unwarranted. For larger projects, Connecticut should develop renewable energy capacity using RFP processes and the long-term “contract for differences” structure developed by the Department of Public Utility Control pursuant to Connecticut General Statutes § 16-243u. Such processes have led to the financing and development of new, efficient peaking capacity in Middletown, Devon, and New Haven. The financing for the peaking plants occurred during what was perhaps the worst financing environment since the Great Depression because of the excellent contractual design. Under this structure, renewable energy plants would have a strong opportunity to earn a reasonable rate of return, but ratepayers would be protected from paying for excessive profits that can occur at times due to market rule design flaws or unexpected occurrences. Conversely, the renewable energy plants would be protected from a sudden loss of expected revenues, and this protection benefits the project, ratepayers, and financiers by avoiding payments to insure against undue risks.

As an aside, OCC notes that feed-in tariffs, if used, could and arguably should be structured as contracts for differences as well, to avoid running afoul of FERC’s exclusive jurisdiction over wholesale power rates. Contracts for differences are financial contracts that do not lead to the direct sale or purchase of power.

Since such renewable energy contracts or tariff arrangements would be entered into as a matter of state public policy and on behalf of all ratepayers, the costs and benefits of such contracts/tariffs should be designed to flow equitably to all Connecticut ratepayers through a non-bypassable charge on ratepayer bills.

Now, some might say that this approach of promoting renewable energy projects that fit under a certain premium level is a way of not building renewable energy at all. OCC has a different view. The premiums can be set at high or low levels and adjusted to reflect the circumstances. If a premium of X fails to yield significant renewable energy and fossil fuel pricing were to increase in unexpected ways, the premium could be change to 1.5X and a new RFP process held to develop projects that might come under that premium. Moreover, an analysis of the costs of new renewable energy projects should not ignore the potential price suppression benefits of renewable energy on regional markets. For example, a wind project may look significantly more expensive than a natural gas project on a capital cost per megawatt basis, but the wind project, since it does

not use fuel, might bid as a price taker in the energy market and possibly avoid the dispatch of a plant with expensive fuel costs, thereby mitigating the market clearing price. Such factors are not at all easy to quantify but conservative estimates of these effects can be used.

In addition to request for proposals for large renewable projects and feed-in tariffs for small renewable projects, OCC would also support in principle the continuation of pilot projects for new technologies.

As to the list of benefits of completing renewable energy projects, such benefits would include economic development, air quality, power reliability, and promotion of new and sustainable technologies. The hedge benefits of renewables (building renewables as a hedge against fossil fuel prices) have declined of late due to the stabilization of natural gas supply and pricing, but the hedge benefits may still exist on a long-term basis. OCC does not have a firm preference as to which of these benefits should get priority, but OCC has a special interest on behalf of its ratepayers in replacing old, inefficient power plants with new, efficient and cleaner plants.

2. How should we define our approach to renewables policy to make it most attractive and rewarding to market participants?

In terms of building new capacity, OCC is fairly certain, based on its experience to date, that the regional markets coupled with the RPS requirements will not lead to the construction of renewable energy plants where needed, when needed, particularly if “where needed” is interpreted to include Connecticut. One flaw of the ISO New England energy markets is the flaw that environmental externalities are ignored. Without taking externalities into account, the ISO New England markets, even if they worked perfectly, might only lead to natural gas plants being built and financed. The Regional Greenhouse Gas Initiative and RPS requirements have not been able to overcome this flaw, and renewable energy credit (“REC”) income has proven too volatile in price to lead to effective financing and project development, in most cases. Thus, we are seeing and will see (most) renewable energy plants built if and only if they have a long-term power purchase agreement. Under such a ratepayer backstop, which OCC accepts (see # 1,

above), the value of RECs is not actually leading to project development (the power purchase agreement is doing that), so REC value should come back to the ratepayers.

In other words, under a long-term contract approach, ratepayers are indeed taking on a good deal of the risk of project development and financing, so income streams that are risky or volatile should also be shifted to ratepayers, leaving the project with more stable (and appropriately limited) sources of income.

More generally, though, if RECs are indeed not going to lead to project development, what is their use? They may have little use other than as support for projects that exist today and that rely on REC value to stay in business. If RPS policy is changed significantly, then we should look at a “grandfathering” program to be fair to existing resources.

For most renewable developers, we believe that a long-term contract (for large projects) or a feed-in tariff (for smaller projects) would be very attractive if structured well. With effective regulation such approaches would lead to: (i) renewable projects being built on the ground, not just on paper; (ii) fair compensation for the plant (if well-operated); and (iii) fair costs for the ratepayers.

3. Please describe your “ideal” (renewable) energy policy in Connecticut.

OCC has described one effective policy approach above in the answers to the above two questions. More generally, we should embrace science and abandon “policy by slogan.” “20% by 2020” is a slogan. The level was selected, as far as OCC is aware, without the rigorous analysis that is now a hallmark of Connecticut electricity decision-making processes, including the integrated resource planning process and the request for proposal process that led to the aforementioned peaking plants. Under OCC’s recommended approach, you basically build renewable energy projects that are priced under selected cost premiums and decline to build projects that are above the premiums. Connecticut should indeed want to build renewable energy at some costs, but not at all costs.

Moreover, we should acknowledge the limited benefits to Connecticut of renewable energy projects to our North and East. OCC fears that the cost of building transmission lines to renewable energy projects well to our north and east will lead to a

large flow of dollars out of Connecticut. Connecticut would share in any reduction of global carbon emissions of such projects but there would be little or no direct benefits to Connecticut's air quality from such projects. Ideally, if Connecticut's dollars are going to support out-of-state renewable energy projects, it would be better for such projects to replace some coal capacity to our west and south, as the prevailing winds come from those directions.¹

In OCC's view, the RPS approach ideally would be replaced with the "acceptable premium" approach outlined above. The RPS is simply not likely to lead to projects where we would like them or when we would like them, provides no assurance of project development and provides only limited protection against excessive costs. RECs and RPS were a valiant effort to create a market and let the "invisible hand of the market" pick projects. However, we can better harness the benefits of competition by conducting "request for proposal" processes for long-term contracts. In either the REC approach or the RFP approach, the demand is manufactured, so there is no loss in theoretical validity from the RFP approach. What you gain from the RFP approach is greater certainty of project development and better cost containment for ratepayers. This in turn could help Connecticut achieve the critical energy goal of a more diversified portfolio without material increases to the price of power.

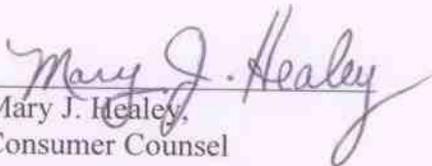
4. In addition, please provide any other comments or suggestions that you would like to share with the Committee.

OCC appreciates the opportunity to provide these comments and looks forward to contributing to further discussions on the CEAB RPS Review Subcommittee.

¹ Prior versions of the RPS statute allowed renewable sources in Pennsylvania, New Jersey, Maryland and other nearby states to count as Class I (without requiring that the energy be actually delivered to New England). To the extent that the change in the statute will lead to Maine projects rather than Pennsylvania projects, for example, that may prove not to be in Connecticut's best interest from an air quality perspective.

Respectfully submitted,

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