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Via Electronic Delivery

June 4, 2018

Hon. Kathleen H. Burgess
Secretary
New York State Public Service Commission
Three Empire State Plaza
Albany, New York 12223-1350

Re: Case 18-E-0071 - In the Matter of Offshore Wind Energy.

Dear Secretary Burgess:

Please find attached for filing in the above-referenced case the Comments of Independent Power Producers of New York, Inc.

Respectfully submitted,

READ AND LANIADO, LLP
Attorneys for Independent Power Producers
of New York, Inc.

By: *David B. Johnson*
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NEW YORK STATE
PUBLIC SERVICE COMMISSION

Case 18-E-0071 - In the Matter of Offshore Wind Energy.

COMMENTS OF INDEPENDENT POWER PRODUCERS OF NEW YORK, INC.

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Dated: June 4, 2018

NEW YORK STATE
PUBLIC SERVICE COMMISSION

Case 18-E-0071 - In the Matter of Offshore Wind Energy.

COMMENTS OF INDEPENDENT
POWER PRODUCERS OF NEW YORK, INC.

I. INTRODUCTION

On April 11, 2018, the Secretary of the New York State Public Service Commission ("Commission") issued a notice inviting comments "on the adoption of a regulatory program to encourage the procurement of electricity from new offshore wind generating facilities by New York State consumers."[1] In the Notice, the Commission proposed to adopt a goal that would require New York electricity consumers to purchase the output of 2,400 MW of new offshore wind generating facilities by 2030 to assist the State in meeting its goal of reducing statewide greenhouse gas emissions by 40% by 2030 ("40% by 2030 goal"). The Notice stated that the Commission proposes to "jumpstart" the deployment of new offshore wind generating facilities by requiring all load serving entities ("LSEs") serving retail customers in New York to annually procure Offshore-wind Renewable Energy Credits ("ORECs") associated with up to 800 MW of new offshore wind generation facilities from the New York State Energy Research and Development Authority ("NYSERDA") (the "ORECs Proposal").

The Notice proposed various options for NYSERDA's procurement of these attributes through solicitations it would conduct in 2018 and 2019. NYSERDA described many of these

[1] Case 18-E-0071, *In the Matter of Offshore Wind Energy*, Notice Soliciting Comments (Apr. 11, 2018) ("Notice"). A Notice of Proposed Rulemaking containing the same text in the Notice was published in the State Register on April 4, 2018 (SAPA 18-E-0071SP1).

procurement options as well as others in greater detail and assessed their associated benefits, costs, legal risks and implications in its "Offshore Wind Policy Options Paper."[2]

Pursuant to the Notice, Independent Power Producers of New York, Inc. ("IPPNY") hereby submits its comments on the Commission's proposals.[3] IPPNY is a not-for-profit trade association representing the independent power industry in New York State. Its members include nearly 75 companies involved in the development, operation, and ownership of electric generators and the marketing and sale of electric power in New York's electricity markets. IPPNY represents numerous companies that invest in and sell various energy products in New York using both traditional generation and renewable energy resources, such as wind. IPPNY's fundamental interest is in the continued development and enhancement of reliable and efficient integrated regional wholesale competitive electricity markets. With respect to the offshore wind energy proceeding, IPPNY's interest lies mainly in ensuring that the Commission's offshore wind energy policies are developed in a manner that are consistent with, and do not undermine in any respect, the functioning of non-discriminatory, competitive energy markets in New York and its surrounding regions.

As discussed below, the most efficient and cost-effective way to achieve a carbon reduction goal without harming the New York Independent System Operator, Inc.'s ("NYISO") wholesale competitive electricity markets with out-of-market compensation to uneconomic resources would be by adopting a market-based approach that provides a single, market-wide carbon price that internalizes a consistent value for carbon into the NYISO's competitive wholesale energy market prices. The NYISO is currently working with Department of Public

[2] 18-E-0071, *supra*, Offshore Wind Policy Options Paper (Jan. 29, 2018) ("Options Paper").

[3] IPPNY's comments do not necessarily reflect the views of individual members of IPPNY.

Service and NYSERDA staff, market participants, and other stakeholders to develop such an approach that would add the full carbon cost to the energy bids of carbon-emitting resources into the NYISO's competitive wholesale energy market (the "Carbon Adder"). Until a Carbon Adder is implemented, new offshore wind energy facilities should be required to compete directly with all other new qualifying renewable energy resource technologies in the central procurement solicitations that NYSERDA is required to hold for Tier 1 RECs pursuant to the Commission's Clean Energy Standard order.[4]

The Commission should reject the ORECs Proposal because it would require NYSERDA to hold solicitations to acquire renewable attributes in which only offshore wind energy facilities would be eligible. The ORECs Proposal is an unreasonable and unnecessary departure from the Commission's long-standing policy that new qualifying large-scale renewable technologies compete against each other on a fair and non-discriminatory basis to ensure the selection of the most cost-effective assets to meet the State's greenhouse gas reduction goals.

If the Commission decides to adopt the ORECs Proposal, any procurement obligation should continue to utilize the structure that has successfully been in place for more than a decade—RECs purchased on a fixed-price basis. However, considering competitive market designs are being developed to internalize the value of carbon emissions reductions in wholesale energy prices, these agreements should be designed to avoid a double payment whereby an offshore wind project would be compensated for its carbon emission reduction benefits by NYSERDA and through the NYISO's wholesale energy market. If, however, the Commission decides to adopt procurement mechanisms that reduce energy price risk to offshore wind energy

[4] Case 15-E-0302, *Proceeding on Motion of the Commission to Implement a Large-Scale Renewable Program and a Clean Energy Standard*, Order Adopting a Clean Energy Standard (Aug. 1, 2016) ("CES Order").

developers, it, at a minimum, must do so in a manner that preserves a developer's incentive to respond to market prices, such as through the proposed Index OREC, Forward OREC, Fixed/Index OREC, or Capped OREC.

The Commission should reject the Market OREC and, although not proposed in the Notice, the Bundled PPA and Split PPA procurement options described in the Options Paper. As IPPNY has long documented, bundled PPAs and so-called contracts for differences (especially those of long duration), such as the proposed Market OREC, whereby compensation to a developer for its attributes varies inversely with its market revenues, could insulate offshore wind energy developers from competitive market price signals and further harm the already fragile NYISO wholesale competitive electricity market. Over the past two decades, IPPNY has consistently emphasized the importance of all suppliers being subject to, and thus having a stake in, accurate and efficient market clearing prices. The procurement of offshore wind energy with State incentives should not cause or contribute to resources bidding at times or at levels that would produce out-of-merit dispatch or otherwise alter the current practice of operating the electric system on the basis of economic dispatch subject to meeting reliability concerns.

IPPNY was pleased to see that the Commission's Notice excluded the Utility-Owned Generation ("UOG") procurement option that was set forth in the Options Paper and, while NYSERDA included it, NYSERDA also recognized the Commission's determination in the CES Order that UOG could inhibit entry by other market participants thereby stifling competition and leading to higher costs over the long run.[5] IPPNY is, however, concerned that NYSERDA suggested in the Options Paper that there may be "a limited role" for UOG "to reflect the specific

[5] *See* Options Paper at 30-31.

early development challenges of the U.S. offshore wind sector."[6] In the event that some parties support this option in their comments, the Commission should reject it on the same grounds as it did in its CES Order.

Nothing has changed in the intervening eighteen months since the CES Order was issued. Indeed, it is precisely because offshore wind generation projects face unique complexities that no steps should be taken that would hinder participation, particularly given the fact that the utilities do not have any expertise to bring to this area and their participation is likely to raise interconnection and other concerns. Permitting UOG in connection with this program would, thus, be a major step backward from years of Commission policy supporting robust competitive electricity markets in New York by generally prohibiting utilities from owning generation.[7] UOG is contrary to the Commission's long-standing pro-competition policies implemented over the past twenty years that correctly have recognized private investors have a greater incentive to lower costs than utilities which are supported by cost-of-service regulation, private investors and their shareholders should bear the risks of generation ownership, and transmission and distribution ("T&D") should be separated from generation to eliminate the potential that T&D utilities that own generation could exercise vertical market power ("VMP") to thwart participation by other market participants to the detriment of the ongoing development of wholesale competitive electricity markets and, ultimately, consumers.[8]

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[6] *Id*. at 31.

[7] The two exceptions to the Commission's policy were permitted based on the specific fact pattern presented as follows: (i) retention by Consolidated Edison Company of New York, Inc. ("Con Edison") of a "bundle" of generating assets to support its steam system operations; and (ii) the limited wind generation development found by the Commission to be required to support Iberdrola's acquisition of two of New York's distribution utilities.

[8] Cases 96-E-0900 et al., *In the Matter of Orange & Rockland Utilities, Inc.'s Plans for Electric Rate Restructuring Pursuant to Opinion 96-12*, Statement of Policy Regarding Vertical Market Power (July 17, 1998) ("VMP Order"); *id.* at Appendix I ("VMP Statement").

II. THE COMMISSION SHOULD NOT ADOPT THE ORECS PROPOSAL.

In its Notice, the Commission proposes to adopt a goal to incent the deployment of 2.4 GW of new offshore wind generating facilities by 2030 to assist the State in meeting its 40% by 2030 goal. The Commission proposes to "jumpstart" the deployment of offshore wind generation by requiring NYSERDA to conduct solicitations in 2018 and 2019 to procure ORECs associated with up to 800 MW of new offshore wind generating facilities through 25-year contracts.

As IPPNY demonstrated in its comments in the Clean Energy Standard case, the most efficient and cost-effective way to reduce carbon emissions in the energy industry would be to expeditiously revise the NYISO's tariffs to implement a Carbon Adder. The Carbon Adder approach recognizes environmental attributes must be compensated and establishes a visible value for low- or zero-emission resources, creating an efficient and cost-effective means for all producers and consumers to factor the cost of emissions into economic decision-making in ways that spur innovation, minimize the cost of controlling emissions, maintain electricity system reliability, and work in harmony with the least-cost dispatching principles that are critical to the proper operation of the NYISO's wholesale competitive electricity markets.

If the full cost of carbon was incorporated into NYISO commitment and dispatch signals, it would provide a better representation of the carbon impact of different resources based upon the actual benefits of their location and generation profile. It also avoids the harm from artificial price suppression resulting from below-cost offers of capacity from resources that are only in the market because of out-of-market payments. Out-of-market compensation to otherwise uneconomic resources is an ongoing and significant threat to, and undercuts the sustainability of, the NYISO's organized electricity markets. The result of artificial price suppression is that the NYISO's markets will not be able to provide the necessary price signals to incent the

maintenance and development of existing and new resources that are necessary to meet reliability needs, resulting in the need to resort to regulated, cost-based supply rather than market-based supply.

Until a Carbon Adder is implemented, new offshore wind energy facilities should be required to compete directly with all other new qualifying renewable energy resource technologies in NYSERDA's Tier 1 REC procurements. The Proposal did not provide any justification demonstrating why NYSERDA should conduct solicitations for an additional 800 MW of renewable attributes from only new offshore wind generating facilities separate and apart from the solicitations that the Commission required, in its CES Order, NYSERDA to conduct for renewable attributes from all other new qualifying large-scale renewable technologies. In its Options Paper, however, NYSERDA asserted that "offshore wind challenges" require that offshore wind generating facilities be procured via "a competitive procurement mechanism which seeks only offshore wind proposals, with commensurate volumetric load-serving entity (LSE) obligations, ramping up to the goal of 2.4 GW by 2030."[9] NYSERDA contended that the cost of offshore wind development is the principal challenge at least in the early stages of the development of this technology.[10] NYSERDA claimed that, while the initial offshore wind projects built in the U.S. are projected to cost more than typical land-based projects, it has conducted analysis that projects the costs of offshore wind are expected to be lower than the

[9] Options Paper at 5.

[10] *Id.*

costs of Tier 1 RECs associated with other large-scale renewable technologies by 2030 if New York pursues the 2.4 GW deployment goal.[11]

The ORECs Proposal is a significant and unjustified departure from the Commission's long-standing policy that new qualifying large-scale renewable technologies compete against each other on a fair and non-discriminatory basis to ensure the selection of the most cost-effective project within such process. Since the Commission adopted the Renewable Portfolio Standard ("RPS"), its policy with respect to the procurement of attributes from new large-scale renewable resources is that such resources should sell their attributes on a technology-neutral basis, *i.e.*, no renewable technologies are given a preferential treatment within the out-of-market process. The Commission has continued this core technology-neutral policy in its CES Order and in its Reforming the Energy Vision ("REV") and related proceedings which incent the development of distributed energy resources.

A procurement mechanism that provides a single technology type an opportunity to earn greater compensation than all other renewable technologies distorts such procurement processes, unfairly favors that technology, and increases costs to consumers. If implemented, the ORECs Proposal would provide offshore wind generation with an artificial advantage over other renewable resources and would set an unfavorable precedent whereby the Commission would pick specific winners and losers in its procurement processes based on their technology type even though selection of the favored technology will result in higher costs to New York electricity consumers.

The higher costs will be realized either through reduced total megawatt-hours procured under each solicitation or through additional solicitations needed to reach the same megawatt-

[11] Options Paper at 20.

hours procurement level. If the given pool of dollars available from LSEs for REC procurements in a given year remains the same as it is under today's program, NYSERDA will not be able to procure as many renewable attributes as it otherwise would, since a certain portion of those renewable attributes associated with offshore wind generation will likely cost NYSERDA, and New York's electricity consumers, more. Alternatively, if NYSERDA decides to procure a fixed level of renewable attributes, it will need to increase the price charged to LSEs to procure those attributes as compared to the amount required to procure the same number of attributes under the current CES. Both of these scenarios will result in an identical outcome: a higher cost of renewable resources for New York electricity consumers and further deterioration of the NYISO's competitive wholesale market.

The Commission has rejected numerous requests in the past to provide greater incentives or other preferences to particular technologies because it would cause consumers to pay more for less attributes. For example, the Commission rejected a proposal to provide smaller-scale wind projects a 1.5 multiplier for bids received in NYSERDA's Main Tier solicitation in the RPS:

> [T]he Main Tier program is designed to be technology neutral and reward developers that offer bids for renewable attribute that are lower in cost than others. We have stated in the past that the Main Tier is not intended to force contribution by, or as is done in the Customer-Sited Tier, apportion financial support to, any particular technology. Eligible technologies are reached in the Main Tier based on where the costs, and therefore bids, fall on a supply curve of all the competing technologies in relation to the demand created in the RPS Program. To provide a multiplier on the bid price for small wind projects would undermine this principle by creating an

> artificial advantage for such projects and would result in ratepayers paying higher prices for fewer MWhs of energy production.[12]

In its Options Paper, NYSERDA claims that many benefits would result from achieving the 2.4 GW goal: (i) it will be a major portion of the renewable generation needed for New York to meet the 40% by 2030 goal; (ii) emissions reduction benefits amounting to approximately $1.9B (net present value); and (iii) considerable economic development and public health benefits for New York.[13] NYSERDA's implication that these benefits would be lost unless New York "jumpstarts" the deployment of 2.4 GW of offshore wind generation with preferential compensation is utter speculation.[14] NYSERDA pointed out efforts by other states to develop offshore wind generation.[15] Nowhere in its Options Paper did NYSERDA explain why these other states' efforts will not provide the necessary "jumpstart" of offshore wind generation development to bring the economies of scale that NYSERDA believes is necessary to reduce the costs of offshore wind generation attributes below the costs of Tier 1 RECs associated with other large-scale renewable technologies.

It appears the major driver of the ORECs Proposal is for New York to be first in developing large-scale offshore wind generation, despite the large premium that electricity consumers will likely pay for this dubious honor. NYSERDA's proposal that offshore wind generators be awarded contracts with NYSERDA for ORECs for 25-year terms means that electricity consumers would likely be required to pay huge premiums for offshore wind generation over other renewable technologies well past the time that the cost of the offshore

[12] Case 03-E-0188, *Proceeding on Motion of the Commission Regarding a Retail Renewable Portfolio Standard*, Order Authorizing an Increase in the Maximum Project Incentive for the On-Site Wind Program in the Customer-Site Tier (Feb. 14, 2013), at 9–10.

[13] Options Paper at 4–5, 19–20.

[14] *See id.* at 24.

[15] *Id*. at 14–16.

wind generation has plummeted to a level that is competitive with other renewable resources. That cost, in conjunction with the adverse impact on the NYISO's competitive energy market and the concomitant out-of-market actions and costs required to maintain reliability, will create an untenable situation for New York consumers and businesses.

Considering the lack of evidentiary support, NYSERDA's analysis that 2.4 GW of offshore wind generation will be needed to be deployed through discriminatory procurements of ORECs should be given little weight. NYSERDA's analysis was based on the history of "dramatic" cost reductions for offshore wind generation development in Europe in recent years.[16] NYSERDA states that, in Europe, "in many cases offshore wind is cost-competitive with land-based renewables," and that the cost reductions in Europe "depended to a material extent on local learning and local infrastructure development resulting from economies of scale."[17] This is not evidence of what needs to be done in New York.

NYSERDA's analysis fails to consider that it should be much less costly and take much less time to reach the level of cost reductions in Europe because much of the technological hurdles of siting offshore wind generation have already been overcome there. Many factors affect the speed with which an offshore wind generation development industry can be brought to scale in a certain locale: including but not limited to wage levels, skills availability, utility rates, taxes, subsidies, shipping costs and reliability, local productivity, and supervision costs.

[16] *See id.* at 20.

[17] *Id.* at 5.

NYSERDA did not address any of these complex factors in its analysis. Thus, the development "learning curve" in the U.S. could be much shorter than that which took place in Europe.

Consistent with the Commission's policy to require all qualifying large-scale renewable technologies to be procured and evaluated in a consistent process to receive State incentives, the Commission should reject any proposal that would provide any preferential treatment for offshore wind generation with respect to other qualifying large-scale renewable generation.

Thus, until a Carbon Adder is implemented, new offshore wind energy facilities should be procured in the same process as all other new qualifying renewable technologies in the central procurement solicitations that NYSERDA is required to hold for Tier 1 RECs pursuant to the CES Order.[18] Resources currently bid into NYSERDA's competitive solicitations are evaluated based upon a number of criteria in order to ensure they bring the greatest benefit to the State and electricity consumers while meeting public policy goals. Implementing a special procurement solely for a specific technology will undermine the competitive nature of the CES solicitation program and negatively impact consumers.

III. IF THE COMMISSION DECIDES TO ADOPT THE ORECS PROPOSAL, IT SHOULD ADOPT THE FIXED REC PROCUREMENT OPTION AND REJECT ANY PROCUREMENT APPROACH THAT WOULD INSULATE OFFSHORE WIND GENERATION FROM REAL-TIME WHOLESALE ENERGY MARKET PRICES.

In its Notice, the Commission listed six options for NYSERDA's procurement of ORECs.[19] The Commission should adopt the Fixed OREC option if the Commission adopts the ORECs Proposal. As stated in the Notice, the Fixed OREC option is similar to the Commission's approach used for NYSERDA's Tier 1 REC solicitations and has also been used

[18] *See* CES Order at 111–13.

[19] Notice at 4–7.

by NYSERDA under the RPS since its inception.[20] While New York's current approach for Tier 1 REC solicitations has negatively impacted, and continues to negatively impact, the NYISO's competitive wholesale energy markets, it is the "best" approach among the discriminatory procurement options proposed.

The Commission should reject the Market OREC and, although not proposed in the Notice, the Bundled PPA and Split PPA procurement options described in the Options Paper. As IPPNY has long documented, bundled PPAs and so-called contracts for differences ("CFDs"), such as the proposed Market OREC, whereby compensation to a developer for its attributes varies inversely with its *actual* market revenues, would insulate offshore wind energy developers from competitive market price signals and harm the wholesale competitive electricity market.[21] The procurement of offshore wind energy with State incentives should not divorce bidding incentives and operating practices from market clearing prices causing or contributing to out-of-merit dispatch or otherwise altering the current practice of operating the electric system on the basis of economic dispatch subject to meeting reliability concerns.

IPPNY has long opposed basing incentive programs on pricing mechanisms that insulate any supplier from competitive market prices, such as CFDs and long-term fixed price PPAs.[22] While NYSERDA suggests that the bundled PPA structure would provide a long-term hedge on energy prices for retail consumers,[23] consumers will be fully exposed to higher payments when energy prices fall as predicted by NYSERDA. This is particularly problematic given that the "long term" in this case will be 25 years, well beyond the period of time that energy price

[20] *Id.* at 4.

[21] *See, e.g.*, Case 15-E-0302, *supra*, IPPNY Comments (Aug. 12, 2015), at 16–22.

[22] *See, e.g., id.*

[23] Options Paper at 27.

forecasts could reasonably be expected to have any significant degree of accuracy. Bundled PPAs shift the energy price risk from developers, who are in the best position to forecast and manage risk, to consumers. Indeed, the exposure to such risk will significantly undercut—if not entirely eliminate—any claimed benefits associated with reduced financing costs that potentially could arise under this option and indisputably will eviscerate the benefits of competitive markets.

Equally important are the adverse system and competitive market impacts that will result if such a structure was put into place. IPPNY has opposed bundled PPA contracts because they can make suppliers participating in these programs indifferent to market prices that may signal the need to reduce output or curtail service to ensure the reliability of the electric system. By its very design, the wholesale electricity market structure in New York values energy when and where it is needed most. Divorcing the payment to the supplier from the market price results in the supplier choosing to keep operating when its output may be harming the system. If suppliers are not responsive to market price signals and continue to operate when their output may threaten system reliability, the NYISO is forced to take additional out-of-market actions to maintain the reliability of the system. The costs of the NYISO's actions are not reflected in market prices but are recovered in additional uplift payments from consumers, an additional form of cost exposure that generally cannot be hedged. This activity distorts competitive market price signals, harms the efficiency of the market, and is more expensive for consumers.

Generally, traditional generators within the NYISO bid positive values for incremental energy because they can save fuel costs by reducing their generation levels. Any time the NYISO markets produce a negative price, the market is indicating that one or more transmission elements on the electric system are overloaded and the NYISO does not have sufficient supply that can be backed down quickly enough to relieve the overload. In those instances, the only

way that the NYISO can relieve the overload is to back down the cheapest supply. It is important at these times that suppliers' payments reflect the NYISO prices so that it will be in their economic interest to respond to the negative prices. Requiring offshore wind generation to be subject to real-time market prices ensures that they will have the correct financial incentives to reduce energy production when such action is needed by the system.

If the Commission decides to adopt procurement mechanisms that reduce energy price risk to offshore wind energy developers, it must, at a minimum, do so in a manner that preserves a developer's incentive to respond to market prices. The proposed Index OREC, Forward OREC, Fixed/Index OREC, and Capped OREC would all ensure that an offshore wind generator would have the incentive to respond to real-time market prices because it would adjust prices for ORECs based on average energy market prices rather than the actual market prices that the generator is paid. Thus, to recognize the unique complexities of this technology and its nascent state while also limiting the impacts to the competitive markets, IPPNY respectfully requests the Commission choose one of these four OREC options to be the procurement mechanism for the offshore wind generation program if the Commission does not adopt the Fixed OREC option.

IV. THE COMMISSION MUST NOT WEAKEN ITS LONG-STANDING POLICY PROHIBITING UOG.

While not proposed in the Notice, NYSERDA proposed in its Options Paper a UOG procurement option under which "[o]ffshore wind developers would develop, design, build, and potentially operate offshore wind facilities; and once completed, project ownership would be transferred to the utility or utilities."[24] While NYSERDA recognized that the Commission has just recently rejected the UOG procurement option once again in its CES Order, NYSERDA

[24] *Id.* at 6.

states that "there may be a limited role for this structure to reflect the specific early development challenges of the U.S. offshore wind sector."[25]

As the Commission has found and IPPNY has consistently demonstrated in various proceedings,[26] energy services should be provided cost-effectively by private developers on a competitive basis rather than by utilities through rate-of-return regulation. This approach ensures that private investors, not captive ratepayers, bear investment risks. It also ensures that utilities are not able to exercise VMP to the detriment of competitive markets and consumers. The Commission should reaffirm its commitment to these principles by continuing its long-standing prohibition on UOG.

A. UOG Shifts Investment Risks Back to Captive Ratepayers.

Market-based mechanisms are the best means of procuring resources and services in the most efficient manner. In its seminal opinion issued in 1996 to introduce competitive electric markets in New York State, the Commission adopted its policy endorsing, *inter alia*, the creation of a competitive wholesale generation market.[27] In Opinion 96-12, the Commission determined that competitors would have a greater incentive to lower costs than utilities under a cost-of-service regulatory regime, which would inure to the benefit of New York's consumers.[28] The Commission also recognized in Opinion 96-12 that the most efficient means of selecting new

[25] *Id.* at 8.

[26] *See, e.g.*, Case 14-E-0302, *Petition of Consolidated Edison Company of New York, Inc. for Approval of Brooklyn Queens Demand Management Program*, Comments of Independent Power Producers of New York, Inc. (Oct. 6, 2014), at 2–3, 14–15; Case 14-M-0101, *Proceeding on Motion of the Commission in Regard to Reforming the Energy Vision*, IPPNY Comments (Sept. 22, 2014), at 6, 12–15; Case 14-M-0101, *supra*, IPPNY Comments (July 18, 2014), at 8–16.

[27] Cases 94-E-0952 et al., *In the Matter of Competitive Opportunities Regarding Electric Service*, Opinion and Order Regarding Competitive Opportunities for Electric Service, Opinion 96-12 (May 20, 1996), at 32 ("Opinion 96-12").

[28] *Id.* at 30.

resources is via the competitive market. Further, the Commission found that one of the primary benefits of competitive markets is that investment risks would shift from captive utility ratepayers to private investors.[29]

If, in addition to the other out-of-market activities that are threatening the NYISO wholesale competitive markets, utilities are allowed to develop or acquire an interest in cost-of-service, rate-regulated large-scale renewables, ratepayers ultimately will be put back in the position of being at risk to shoulder the cost overruns of such projects. As history demonstrates, the risk of such cost overruns and ratepayer harm is very real. For example, Con Edison's East River Repowering Project, prompted by needs on Con Edison's steam system, had an initial estimated cost of $406 million. However, ratepayers were required to bear final costs of $788.3 million, almost a 100% overrun of original cost estimates.[30] Similarly, Rochester Gas and Electric Corporation's ("RGE") construction of its Rochester Transmission Project (albeit a transmission project) was projected to cost approximately $75.4 million when initially authorized.[31] The estimates subsequently ballooned to $125 million, a 60% increase. In the case of a merchant renewable facility or other resource, private investors bear the risk of loss, not consumers. Because they do not have the luxury of an assured regulated revenue stream to cover their costs, they are forced to be more efficient. Problems such as cost overruns and negative impacts on the competitive markets can be avoided by continuing the Commission's policy recently reaffirmed to prohibit utilities from owning cost-of-service, rate-regulated generation assets in this program.

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[29] *Id.* at 30–31.

[30] Case 05-S-1376, *Consolidated Edison Company of New York. Inc.*, Order Determining Revenue Requirement and Rate Design (Sept. 22, 2006), at 6.

[31] *See* Case 03-T-1385, *Rochester Gas and Electric Corporation*, Order Granting Certificate of Environmental Compatibility and Public Need (Dec. 16, 2004), at 4.

B. UOG Chills Private Investment.

The Commission's decision more than two decades ago to restructure New York's energy markets from vertically integrated monopolies to a competitive wholesale and retail market structure was based on the fundamental economic principle that competition brings forth efficiencies, technological advancements, innovation, savings, and other benefits, which are unlikely to occur as effectively, if at all, absent the motivation provided by such markets.[32] The Commission's basis for the decision to move towards competitive markets was sound but the follow through has not been consistent with concepts behind restructuring. Properly designed competitive electricity markets (where out-of-market activities are not prevalent) lead to more efficient operations, lower utility bills for customers than would have occurred under the former centralized framework, a better climate for companies seeking to do business in the State, and a healthier state economy overall.

Accordingly, at a minimum, offshore wind energy developers should be required to compete to provide products that benefit consumers at a lower cost than can be provided by utilities. As established, *supra*, the chosen procurement option should require the developers to bear risk. However, if utilities are allowed to own offshore wind generation and recover costs via cost-of-service rates, it will not only harm the competitive electric markets in the State, as discussed below, but it will also further chill the already fragile merchant investment community from making future investments in the State, which would do immense harm to the market. As private investment is discouraged, utilities, which are typically unresponsive to price efficiencies and reluctant to innovate, will dominate the ownership of offshore wind generation. Once this cycle begins, it will become a self-fulfilling prophecy. Less merchant involvement will produce

[32] Opinion 96-12 at 26.

more monopoly domination, which, in turn, will produce even less merchant investment. This dynamic will not end once the first few solicitations are completed as NYSERDA suggests. It will, instead, define the structure of this part of the generation portfolio, *i.e.*, a market will never develop.

It is impossible to fairly compare the costs and benefits of a proposed project that will obtain cost-of-service, rate-based recovery with a private developer's proposed project that must rely on attribute payments and energy and capacity revenues for cost recovery. A project that is willing to cap the total cost exposure to consumers through a combination of REC and properly designed competitive market revenues would ultimately be more beneficial to customers than a cost-based solution that may have a lower initial cost estimate (making it *appear* to be the better choice) but also retains the ability to seek recovery of all costs without limitation.

In addition, it will be impossible to ensure that utilities will accurately disclose all of the benefits a renewable project will provide to their T&D systems. For example, a utility could underbid a non-utility project because it alone knows that its project will delay needed upgrades to its T&D system and can redirect those "savings" to the project that will otherwise reduce the utility's costs and allow it to offer a lower bid. Non-utilities will be at an obvious disadvantage in bidding against utilities if non-utilities, which have far less knowledge of the T&D system than the utilities that own and operate the local distribution systems, are unable to reflect these cost savings in their bids. Therefore, to ensure that utilities have no incentive to hide their T&D system cost savings that will result from an offshore wind generation project and to promote a level playing field generally, utilities should be ineligible from participating in solicitations for these projects.

The Commission has already considered and rejected proposals to allow utilities to own renewable generation. During the 2009 RPS review, the Commission rejected the establishment of a new "Utility-Sited Tier" to promote small, utility-owned solar photovoltaic facilities that integrated renewable energy generation into the distribution system at strategic locations.[33] The Commission reaffirmed its policy prohibiting utilities from owning small-scale renewables, except in very limited circumstances, in its REV policy order. The Commission ruled that "[a] basic tenet underlying REV is to use competitive markets and risk-based capital as opposed to ratepayer funding as the source of asset development. On an *ex ante* basis, utility ownership of [distributed energy resources ("DER")] conflicts with this objective and for that reason alone is problematic."[34] Consequently, the Commission established the "general rule" that "utility ownership of DER will not be allowed unless markets have had an opportunity to provide a service and have failed to do so in a cost-effective manner."[35] As discussed above, the Commission most recently rejected UOG in its CES Order, consistent with its long-standing policies.[36]

There has been no showing that there is a shortage of private developers that will compete to develop offshore wind generation. The experience to date has been that private investment has responded to the call for the development of renewable resources. This

[33] Case 03-E-0188, *Proceeding on Motion of the Commission Regarding a Retail Renewable Portfolio Standard*, Order Authorizing Customer-Sited Tier Program Through 2015 and Resolving Geographic Balancing and Other Issues Pertaining to the RPS Program (Apr. 2, 2010), at 34–35.

[34] Case 14-M-0101, *supra*, Order Adopting Regulatory Policy Framework and Implementation Plan (Feb. 26, 2015), at 67.

[35] *Id.* at 68.

[36] CES Order at 101.

experience should continue to guide the structure and rules for offshore wind generation ownership.

C. The Commission Determined That the Most Effective Way to Allay VMP Concerns Arising from UOG Is to Prohibit UOG.

The Commission's VMP Policy established a rebuttable presumption "that ownership of generation by a T&D company affiliate would unacceptably exacerbate the potential for vertical market power."[37] Consistent with long-standing Commission policy, utilities should continue to be proscribed from owning generation in New York State, including offshore wind. IPPNY has been a strong supporter of the VMP Policy Statement, which requires the separation of generation from T&D utilities to eliminate the potential that T&D utilities could exercise VMP to the detriment of wholesale competitive electricity markets and consumers.[38] The Commission's VMP Policy Statement assures energy market participants considering doing business or making further investments in the State that the Commission is committed to a competitive electric market. The VMP Policy Statement discussed the problem with potential VMP:

> Vertical market power occurs when an entity that has market power in one stage of the production process leverages that power to gain advantage in a different stage of the production process. A utility with an affiliate owning generation may, in certain circumstances, be able to adversely influence prices in that generator's market to the advantage of the combined operation.[39]

The Commission identified the potential for VMP in two instances.[40] First, VMP could be exercised when a utility owns generation in its own service territory. The Commission was

[37] VMP Policy Statement at 1–2.

[38] *Id.*

[39] *Id.* at 1.

[40] *Id.*

concerned that the utility could use its control of the T&D system to favor its own generation or thwart its competition by either lowering competitors' revenues, raising their costs or delaying their projects. Second, VMP could be exercised when a utility owns generation that is located on the high side of a transmission constraint. The Commission was concerned that the T&D utility could use its control of the transmission system to increase constraints and raise the value of its generating assets.

From the outset of its move to a retail competitive model, the Commission found that, in a wholesale or retail competitive model, generation and energy service functions should be separated from T&D functions, wherever feasible, to eliminate concerns related to the exercise of VMP and best meet the interests of ratepayers. The Commission determined that total divestiture of generation was the clearest way to allay concerns about VMP and avoid anti-competitive behavior (such as favored treatment of affiliates and cross-subsidies among affiliates in both competitive and monopoly environments).[41] Finding that separating ownership of generation from T&D was preferable to relying on regulatory controls and enforcement mechanisms because the latter were incapable of timely identifying and remedying the potential for abuse, the Commission established a rebuttable presumption that separation of these functions was required.[42] The first paragraph of the VMP Statement summarized the Commission's findings:

> In creating a competitive electric market, the Commission has viewed divestiture as a key means of achieving an environment where the incentives to abuse market power are minimized. *Recognizing that vigilant regulatory oversight cannot timely*

[41] Opinion 96-12 at 64–65.

[42] VMP Policy Statement at 1.

> *identify and remedy all abuses*, it is preferable to properly align incentives in the first place.[43]

In addition, the Commission stated that divestiture would help create a larger number of competing generating companies, which would result in a more dynamic market.[44]

The Commission, therefore, strongly encouraged the utilities to divest their generation.[45] And it ultimately adopted divestiture as the path forward, a step which ultimately occurred and was sanctioned at the Commission in the utility-specific rate and restructuring cases resulting in the divestiture of the vast majority of generation assets.[46] As established *supra*, to avoid the adverse impacts that would result from the exercise of VMP on both the continued development of competitive markets and, concomitantly, consumers, the Commission subsequently established strict VMP guidelines in the VMP Policy Statement that expressly provide that the proponent of a proposal to own both transmission and generation would face a very high hurdle in its Section 70 proceeding, namely, it must overcome the rebuttable presumption that such dual ownership would unacceptably exacerbate the potential for VMP. The Commission ruled:

> To guard against undesirable incentives, a rebuttal [sic] presumption will exist for purposes of the Commission's Section 70 review of the transfer of generation assets, that ownership of generation by a T&D company affiliate would unacceptably exacerbate the potential for vertical market power. To overcome the presumption the T&D company affiliate would have to demonstrate that vertical market power could not be exercised because the circumstances do not give the T&D company an opportunity to exercise market power, or because reasonable means exist to mitigate market power. Alternatively, the T&D company would need to demonstrate that substantial ratepayer

[43] *Id.* (Emphasis added.)

[44] Opinion 96-12 at 65.

[45] *Id.*

[46] The one notable exception was Con Edison's retention of one generation "bundle" to allow it to continue to meet the needs of its steam system.

> benefits, together with mitigation measures, warrant overcoming the presumption.[47]

The Commission's policy has been implemented with great success. Except in the limited instance of generation associated with addressing the steam system in New York City, the T&D utilities have divested their generation, the vast majority of new generation has been developed by independent power producers, and a competitive wholesale electricity market has been operating in New York for more than two decades bringing consumers significant environmental, economic and efficiency gains.

The Commission subsequently has reaffirmed its VMP Policy Statement since the utilities divested most of their generation. In 2007, the Commission found the joint proposal to support the merger of National Grid and KeySpan to be deficient because it would have permitted National Grid to own generating facilities. In its order addressing the proposed merger, the Commission rectified this deficiency by identifying the additional requirement that, *inter alia*, National Grid must agree to divest the 2,450 MW Ravenswood generating facility portfolio as an express condition to approval of the merger.[48] The Commission explained why it adopted this condition:

> For more than 12 years, this Commission has taken numerous actions to develop competitive markets for generation products in New York. The long-term goal is that customers should be able to obtain generation products by paying prices resulting from a fully competitive generation market in lieu of regulated prices (or rates) based on the costs of generation.[49]

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[47] VMP Policy Statement at 1–2.

[48] Case 06-M-0878, *National Grid PLC & KeySpan Corp.*, Order Authorizing Acquisition Subject to Conditions and Making Some Revenue Requirement Determinations for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (Sept. 17, 2007).

[49] *Id.* at 128.

Finding other proposed mitigation measures insufficient to adequately address VMP concerns, the Commission held, "We agree with IPPNY and others that a decision by us to rely solely on regulatory solutions would signal and in fact would amount to a weakening of our resolve to ensure a competitive generation market and its attendant benefits."[50]

The Commission also reaffirmed its VMP Policy Statement when it conditioned its approval of Iberdrola's acquisition of RGE and New York State Electric and Gas Corporation ("NYSEG") on the divestment of any and all fossil-fueled generating assets in New York State then owned, and the prohibition of the future construction or acquisition of any fossil-fueled generation in New York, by Iberdrola and its affiliates.[51] While the Commission allowed NYSEG and RGE to develop a limited amount of wind generation in their service territories, such action was specific to the facts and circumstances of the merger at hand, was required to support the merger's approval (by providing substantial ratepayer benefits of $275 million) and was contingent upon the requirement that the generation must be owned by affiliates separate from the utilities and the imposition of VMP mitigation measures.[52] These facts are easily distinguishable from the facts here where there are no significant ratepayer benefits being offered by any utilities that could not be provided by private investors to offset the harm that will be caused by the utilities' ability to exercise VMP if they own large-scale renewables. Thus, the Commission should continue to prohibit utilities from owning any generation facilities in New York State, including offshore wind generation, to guard against the exercise of VMP so long as private investors are willing and able to develop projects in New York.

[50] *Id.* at 134.

[51] Case 07-M-0906, *Iberdrola, S.A. et al.*, Order Authorizing Acquisition Subject to Conditions (Jan. 6, 2009).

[52] *See id.* at 95–100, 137.

V. CONCLUSION.

For the foregoing reasons, the Commission should:

(i) reject the ORECs Proposal;

(ii) adopt the Fixed OREC option if it adopts the OREC Proposal;

(iii) reject any procurement option that eliminates a developer's incentive to respond to market prices (i.e., proposed to date, the Market OREC, PPA and Split PPA options); and

(iv) reject the UOG option.

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