COMMENTS OF THE
DEPARTMENT OF THE PUBLIC ADVOCATE
DIVISION OF RATE COUNSEL

Revised Straw Proposal:
New Jersey's Offshore Wind Renewable Energy Certificate ("OREC")

March 26, 2009

1. Introduction

The Department of the Public Advocate, Division of Rate Counsel ("Rate Counsel") would like to thank the Board of Public Utilities ("Board" or "BPU") for the opportunity to present our comments on the Straw Proposal submitted to stakeholders for comment by the Office of Clean Energy ("OCE"), dated March 10, 2009. The purpose of OCE's proposal is to facilitate the goals established in Energy Master Plan ("EMP") released on October 23, 2008 that increases New Jersey's commitment to renewable energy to 30 percent of electricity sales by 2020. An integral part of the EMP has been the call for a minimum of 1,000 megawatts ("MW") of offshore wind capacity to be developed by 2012, and a minimum of 3,000 MW of offshore wind capacity by 2020.

OCE, in its revised straw proposal offered for comment on March 10, 2009, proposes to establish an offshore wind set-aside or "carve-out," within New Jersey's Renewable Portfolio Standard ("RPS"). This carve-out would establish a new tradable credit referred to as an offshore wind renewable energy certification or "OREC." This OREC would have a companion maximum price referred to as an offshore wind alternative compliance payment or "OACP."

Rate Counsel supports what it believes are the overall goals of OCE's proposal: to establish market certainty for the development of offshore wind generation in a challenged financial and economic environment. We do not however, support this specific proposal and find it to be premature since the costs and consequences of this proposal have not been thoroughly addressed. The Straw Proposal includes no estimates of program administrative costs, no estimates of how this approach will reduce the overall costs of delivering offshore wind energy, and most importantly, no estimates of the impact that this proposal will have on rates.

Rate Counsel is particularly concerned that OCE's proposals could have significant implications on Basic Generation Service ("BGS") rates. These issues have not been completely nor thoroughly addressed in the OCE proposal. In the few instances where general proposals have been offered, Rate Counsel believes that OCE's recommendations would result in an immediate increase in rates – driven in large part from the uncertainty associated with this newly-proposed regulation. Rate Counsel is concerned that BGS rates will increase for the following reasons:

(1) OCE's proposal will create a new class of RECs and REC requirements that will increase the cost of RPS compliance.
(2) The creation of a new set of alternative compliance payments will create new uncertainties incenting load serving entities ("LSEs") into "padding" their offers with the maximum offshore wind price ("OACP") to hedge against unexpected offshore wind market outcomes.
(3) OCE's transition proposal to establish a 2013 placeholder value for ORECs will almost certainly result in an increase in rates since no LSE will want to bear the unnecessary risk of under-pricing for this emerging RPS requirement. If LSEs are forced somehow to set prices for their offshore wind requirements at the placeholder value, it sets up the possibility of retroactively re-setting rates to correct for deficiencies in the administratively-determined price.

Rate Counsel is also concerned about the specific proposal to create an entirely new and unneeded framework that sets a troubling precedent and undermines the traditional policy goals of using a RPS to support renewable energy development.

Rate Counsel recommends that the Board utilize an already fully-vetted framework for supporting offshore wind energy development. This framework, established during the course of the Generic Solar Renewable Energy Certificate ("SREC") proceedings, and later expanded in individual electric distribution company ("EDC") filings, could be easily modified to accommodate offshore wind projects.

2. Rate Counsel Opposes Additional Set-Asides

Rate Counsel has opposed establishing new set-asides for renewable energy resources since the advent of the EMP discussion and working group process. Our rationale for opposing these set-asides is quite simple: set-asides result in inefficiencies raising costs to ratepayers. It was Rate Counsel's experience during the course of the EMP working group discussions that the idea of establishing new set-asides was a popular policy proposal for the myriad individual renewable energy developer interests participating in the process. During these discussions, proposals emerged for set-asides for on-shore wind, behind-the-meter wind applications, and bio-fuel generation, to name a few.

Rate Counsel is very concerned that if the Board approves OCE's Straw Proposal it will be moving down a very slippery slope of splitting and balkanizing renewable energy markets into numerous sub-markets with their own tradable credits, their own suppliers, and their own inefficiencies. In such a situation, the state's renewable energy policy digresses into one of various interest groups seeking preferential treatment for their resources at the expense of other renewable energy generation, and ultimately, ratepayers. The Board needs to seek another solution that promotes the efficient development of renewable energy, without compromising the integrity of its own long-term policy.

Rate Counsel is also concerned that by adopting OCE's proposal the Board would inadvertently draw itself into the very trap that has contributed to the current renewable energy underinvestment problem: namely, the regulatory uncertainty resulting from frequent changes in rules and regulations that increases risk for project developers. Adopting OCE's proposal potentially signals to the market that the Board is ready and willing to change or modify its regulatory policies on renewable energy. This creates a moving standard, or set of standards, that challenges renewable energy investment.

While the change in regulatory policy proposed by OCE certainly offers significant benefits to offshore wind developers, it potentially creates adverse impacts on current and potential renewable energy projects that may have been expecting higher REC premiums due to the development of offshore wind energy as the marginal technology setting market prices. Extracting wind energy from the current potential REC resource mix potentially lowers the market clearing price, changing payback and internal rate of return assumptions for existing and emerging projects.

3. OCE's Proposal Would Undermine the Traditional Goals of a RPS

A RPS is typically established to set a renewable energy threshold that all market participants must meet. Suppliers are then required to either develop their own renewable energy production, or purchase renewable energy credits ("RECs") from those qualifying facilities that do not need these credits to meet their own power generation requirements (i.e, those over complying with the standard).

A RPS is commonly thought of as a "market-based" approach for developing renewable energy because it lets the market determine, at the margin, the most cost-effective sources for meeting renewable energy standards. In adopting the RPS, the Board specifically noted:

> New Jersey's RPS proposal for 20 percent renewables by 2020 is not predicated on the development of off-shore wind resources; nor does the RPS, except for the solar set aside dictate what renewable energy technologies are to be developed to meet the RPS requirements. ***The RPS is a market-based rule. It relies on the economic competitiveness of the market in response to the regulation to develop facilities for compliance.***[1]

Under a RPS, a renewable energy supply curve arises in which the least-cost renewable energy resources are developed and deployed first, with higher cost resources either being developed last, or not at all if they are relatively uneconomic. As a result, the least-cost development of renewable energy is thought to be assured through competition.

When the Board modified its RPS in 2006, it established a solar energy set-aside which effectively established a separate solar energy market, and necessitated the

[1] NJ Register, Volume 38, Issue 10, May 15, 2006

development of solar renewable energy credits ("SRECs") for trading purposes for load serving entities ("LSEs"). The Board's approval of the solar set-aside within the RPS created a sub-market which effectively split-off close to 2,000 MW of renewable capacity into its own unique market with its own suppliers and customers. OCE's offshore wind proposal compounds this market segmentation by pulling an additional 3,000 MWs, for a total of 5,000 MW of potential renewable energy capacity away from a traditional RPS approach and into not one – but two separate classes of set-asides.

Competitive markets are defined by a large number of buyers and sellers. Having a large number of buyers and sellers creates competitive pressure for cost reduction and the emergence of substitutes and alternatives. If an LSE, for instance, needs a REC, and finds one offered by an offshore wind facility at $45, while an onshore wind facility is offering RECs at $25, the LSE can choose the lower-cost alternative to meet its RPS requirement.

Creating more and more sub-markets undermines those goals of competitive renewable energy markets by reducing the number of buyers and sellers and creating specific market differentiation. Market differentiation is the first step in moving otherwise competitive markets into those that have the ability to exert various degree of market power since substitutes and alternatives are greatly reduced. Suppliers in these markets become price-makers, not price takers. Competitive pressures to reduce costs are significantly deteriorated, and ultimately consumers (ratepayers) will pay higher rates for projects that may not have existed in a more robust market structure. Rate Counsel cannot support such a mechanism, regardless of how well-intentioned.

4. OCE's Proposal Would Result in New and Potentially Costly Administrative Structure

OCE's proposal creates an entirely new market structure, price discovery institution, and regulatory compliance mechanism that would unnecessarily increase costs to ratepayers. OCE's current proposal would do the following:

- Establish a new offshore wind set-aside within the Board's existing RPS.

- Create a new set of RECs and ACPs, each of which would have their own vintage years. If OCE's proposal is approved, LSEs could have as many as 10 different compliance certificates to manage in order to meet their RPS requirements.[2]

- Create and administer a non-binding price discovery process comprised of a "Request for Pricing Proposals" ("RPP") to set the administrative standard-offer price for ORECs that differs little from a feed-in tariff.

[2]This would include: (1) RECs; (2) ACPs; (3) SRECs; (4) SACPs; (5-7) three different vintage years of ORECs; and (8-10) three different vintage years of OACPs.

- Require the Board to be the supplier administrator that takes title to ORECs and serves as the broker collecting revenues for ORECs from LSEs, and allocating payments to offshore wind developers.

None of these proposals would be necessary if the Board utilized the existing solar contracting approach developed by a broad group of stakeholders for a period now approaching one year. As will be discussed later in our recommendations, by utilizing this approach the Board could:

- Preserve the existing RPS and its market structure without the need for developing a set-aside or new class of RECs and ACPs.

- Leverage the existing competitive bidding process developed by the EDCs for solar energy and what should be lower incremental cost than the stand-alone costs of developing a RPP process proposed by the OCE.

- Leverage the existing solar auction process into a broader renewable energy auction process at what should be a lower incremental cost than the supplier administrative functions included in the OCE proposal.

- Restrict the Board's overall engagement in the mechanics of the renewable energy development process to simply review and approval (and not active participant).

5. OCE's Proposal is Inconsistent with the Board's Past Rejection of Feed-In Tariffs

OCE's Straw Proposal, at its core, is a modified feed-in tariff: a mechanism frequently proposed as a remedy to renewable energy underinvestment, and one just as frequently rejected by the Board due to its inefficiency in determining price. Typically, a feed-in tariff is based upon an administratively-determined standard offer price. Renewable energy developers receive payment for their renewable energy generation at the standard offer price regardless of the fact that their actual costs may be considerably lower than the administratively-determined standard offer price.

The only difference between the OCE proposal and a traditional standard offer is the use of a RPP process to set the appropriate standard offer price. Rate Counsel believes this approach is potentially worse than an administratively-determined price which is at least tempered by regulatory oversight.

OCE's proposal would use a RPP or "indicative offer" approach at discovering price. Under this approach, developers offer non-binding price offers for offshore wind energy.

The approach is non-binding from a price perspective since a high bid does not exclude a developer from later offering ORECs at the lower standard offer price.[3]

Rate Counsel is concerned that this approach may unnecessarily inflate bids, and drive up ratepayer costs, since there is little to no accountability for excessive offers. In such a framework, developers have an incentive to bid-up the price because in doing so, the developer is (a) not excluded from future market participation and (b) can increase profits by inflating its bid, which if followed by all participants, would drive up the OREC supply curve and the market clearing price used to determine the standard offer. If the Board accepts this proposal, some mechanism needs to be included that would reject loosing bids (high offers) from future participation.

OCE's proposal to temper the possibility of inflated bids further highlights the feed-in tariff properties of this approach. By using a consultant, and information from bids in other states and other projects, OCE's proposal digresses into an administratively-determined, regulated price. Thus, ratepayers have the unattractive choice of setting a standard offer price from a faulty bidding system or a potentially inefficient regulatory process. The Board should reject this type of approach much as it has done for solar energy.

6. Rate Counsel is Concerned That The Proposal Could Increase BGS Rates

Rate Counsel is concerned that OCE's proposal will have an unnecessary impact on BGS rates for customers.

First, these BGS rates will increase due to the additional costs for offshore wind energy as well as the compliance and administrative costs included in the OCE proposal. Increases in RPS compliance costs for LSEs, in turn, will be passed along to ratepayers. Unfortunately, the cost of this new compliance standard is unknown since OCE has provided no estimates regarding the administrative costs or the rate impacts of its proposed market design.

Second, the creation of a new set of ACPs ("OACPs") will create an opportunity for LSEs to immediately insulate themselves from risky offshore wind market outcomes. Given market uncertainties about prices, LSEs will have incentives to impute the maximum compliance price for offshore wind to insure against pricing shortfalls.

Third, the transition proposal offered by OCE, for the first round of offshore wind sales in 2013, will result in one of two outcomes. First, it is highly unlikely that OCE will be able to accurately estimate an administratively-determined offshore wind price and some form of *ex post* true-up will likely be required. Second, if OCE sets both OREC and OACP prices, it is highly likely that the OACP price will be selected in order to insure against uncertain market outcomes, and the possibility that LSEs may not be

[3]Assuming that a bidder meets the technical requirements to be a designated facility. There is a binding constraint on the quantity offered by the bidder: they cannot, at a later time, increase the capacity (and energy) from the facility beyond an amount included in the original offer.

reimbursed for choosing some lower price (like the placeholder OREC price) at some later date.

7. OCE's Proposal Excludes A Rate Impact Analysis

A significant shortcoming in OCE's Straw Proposal is the omission of any program cost estimate. It is hard to evaluate the overall merits of this program without reference to program costs. Ultimately, program costs will determine the effectiveness of this program over other alternatives, and most importantly, the rate impacts that will be imposed on ratepayers from this new program.

Rate Counsel would also propose that some form of cost circuit breaker, like that adopted by the Board in the RPS rule modifications for solar, be adopted.

8. Proposals Could Shift Market Risk from Developers to Ratepayers

An earlier version of OCE's straw proposal defined annual OREC prices as the difference between the total OREC price offered by a project and the annualized LMP price for spot (wholesale) market energy. Thus, potential developers would bid an "all-in" price, referred to as a "revenue requirement,"[4] needed to earn a return on their investment. Revenues would include electricity sales revenues and net OREC revenues (presumably the all-in price less electricity sales revenues). The most recent version of the proposal has stricken this formula from the proposal although there are repeated references to "revenue requirements" elsewhere in the OCE proposal, and a statement that "all of the Designated Facility's revenue received from PJM associated with energy produced and delivered (OSW Revenues) will be the property of the BPU." Rate Counsel would request clarification on this pricing proposal to ensure that OREC prices are based only on the additional financial support (i.e., non-electricity sales revenues) needed to develop offshore wind projects.

Rate Counsel would not support a pricing mechanism that includes a true-up for wholesale energy prices. Overall financial support for offshore wind energy comes from a variety of sources that broadly include REC revenues, federal tax incentives, other state and federal incentives, and electricity sales revenues. Rate Counsel believes that wind developers are better suited to bear the risk associated with changes in wholesale energy prices than ratepayers. Including this aspect in any REC pricing proposal does not send strong signals to developers to maximize electricity sales revenues from their facility from non-spot market transactions. The current Straw Proposal notes that OCE will "develop provisions to ensure that the OSW Designated Facilities maximize the sale of electricity to PJM." How OCE intends to make these assurances, and its qualifications to make such assurances, raises exceptional concerns for Rate Counsel.

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[4] A revenue requirement is a regulatory construct designed to develop a set of revenues needed to earn a return on a regulated asset and is not a method of financial modeling typically used by competitive, merchant energy assets. This further highlights the feed-in tariff, regulatory-based approach of the Straw Proposal.

Further, including electricity sales revenues into a formula to determine OREC prices is entirely inconsistent with other forms of renewable energy pricing support including solar energy. For instance, SREC prices are not trued up for actual electricity savings (or sales) revenues under the Board's long term SREC contracting approach. Solar developers only bid the additional (not total) financial support needed to ensure project development. Revenue streams associated with electricity savings, incentives, and tax credits are excluded from the SREC determination.

Rate Counsel recommends that if the Board accepts OCE's proposal, OREC prices be bid at levels needed to support the project net of anticipated electricity sales revenues. It should be up to wind developers to find ways to meet or exceed those anticipated electricity sales revenue targets.

9. Excess Revenues Should be Used to Lower Rates

OCE has proposed that any excess OREC revenues be used as a funding source for clean energy programs supported by all retail customers such as the Clean Energy portion within the Societal Benefits Charge ("SBC") or the Universal Services Fund ("USF"). Rate Counsel is opposed to using excess revenues for anything but credits to the already significant commitments ratepayers are making to clean energy initiatives. The Board should be clear that any excess revenues created from this program will be used to reduce rates, and not to expand, or create additional (higher) incentives for existing clean energy programs beyond their budgeted levels.

10. The Use of Non-Price Evaluation Terms Potentially Biases Outcomes

OCE has proposed using other factors in determining its standard offer price such as the potential that a developer can actually complete a project and an undefined range of economic benefits to New Jersey from any individual project/bid. While Rate Counsel supports specific, and pre-defined participation qualifications, we are concerned that the use of such undefined (or loosely defined) non-price terms is highly subjective and arbitrary. The use of these subjective evaluation parameters potentially biases market outcomes by influencing the standard offer, which in turn impacts market entry, wind energy capacity development, and ultimately, rates.

11. Recommendations: The Current SREC Contracting Approach Should be Modified to Support Offshore Wind Energy

Rate Counsel recommends that the Board direct stakeholders to this process, particularly EDCs, to work collaboratively in modifying the current SREC contracting approach to accommodate offshore wind development. Rate Counsel offers the following suggestions for consideration in this process:

- The Board would direct each of the EDCs to support a target amount of offshore wind energy. There would be no specific ORECs nor any other specific "set-aside."

- The Board and other stakeholders would develop a long-run contracting process for RECs generated by offshore wind energy that, as starting point, follows some variation of the schedule offered by OCE in its Straw Proposal. Some share of the EMP's offshore wind goal can be securitized, while the remaining share is left to the bi-lateral market much like the current plans being utilized for solar energy.

- EDCs would be required to enter into long-term REC contracts with offshore wind energy developers only.

- EDCs would conduct a Request for Proposals ("RFP") process, overseen by an independent third-party administrator, preferably the same third party administrator overseeing the solar energy RFP process.

- Offshore wind developers would submit fixed long term bids for the RECs generated from their projects.

- EDCs would award REC contracts to winning (least cost) bids subject to Board approval. Rejected bids would not be allowed to participate (serve as supply sources) until the next RFP process.

- EDC REC contracts would be for the specific price and quantity offered in the bid, not a market clearing price.

- EDCs would auction RECs to the market in a fashion similar to SRECs.

- EDCs would develop mechanisms, including the use of the Clean Energy Budget within the Societal Benefits Charge ("SBC"), to recover the prudently-incurred cost of the program including:

    - Administrative costs associated with the program.

    - Credits for revenues collected from the REC auction that are in excess of those paid under longer-term REC contracts arising from the competitive bidding process.

    - Charges to make up for shortfalls between revenues generated from the REC auction proceeds and the long-term REC contracted amounts from the competitive REC bidding process.

- The Board will establish a circuit breaker that restricts continued progress in developing future offshore wind energy capacity to some absolute cost, or percent cost increase, constraint.

Rate Counsel believes this approach would be more efficient and transparent relative to the proposal offered by OCE.

Testimony of Doug Pfeister, Bluewater Wind

Offshore Wind Renewable Energy Certificate Hearing

New Jersey Board of Public Utilities

Trenton, NJ

March 26, 2009

Thank you President Fox and Board Staff for giving me the opportunity to provide you comments on the proposed offshore wind carve out in the state rps and establishment of an offshore wind renewable energy certificate (OREC).

My name is Doug Pfeister. I'm project director for New Jersey and head of siting and permitting for bluewater wind of Hoboken. We are an offshore wind developer with active projects in several states in the northeast, including New Jersey and Delaware, where we have the country's first offshore wind power purchase agreement, with Delmarva Power and Light.

Governor Corzine and the Board have shown great leadership on offshore wind, building upon years of study and analysis going back to the 2004 Feasibility Study and the Blue Ribbon Panel on offshore wind and continuing today with the ecological baseline studies due for completion

this year. The state is leading the way on offshore wind – but is doing so upon a rock-solid foundation.

The offshore wind straw proposal we are all considering is the result of an open, inclusive, and responsive stakeholder process seeking to find a policy solution that will bring large-scale renewable energy to New Jersey. That source – the only source available in a state as small and densely populated as New Jersey – is offshore wind. This technology, spinning in Europe since the early 1990s with 30 projects now in operation, is more expensive than conventional power generation but without it, New Jersey cannot serve a significant portion of its load with in-state renewable electricity. A thousand megawatts of offshore wind means that roughly 300,000 households will be powered by pollution-free, renewable electricity. There is just no other option if renewable energy is to lead us into the future in New Jersey.

The straw proposal is intelligently designed so that ratepayers pay only the above-market incremental cost to bring offshore wind parks to construction. The proposal entitles the projects to a fixed price per mwh – but ratepayers pay just the amount not collected in the PJM marketplace. This is a market-based solution that caps the OREC payment and enables ratepayers to reap the benefits of high electricity prices through lower OREC payments. In other words, when wholesale electricity prices are high, OREC prices are low.

Getting this offshore wind policy right is a big opportunity for New Jersey. Getting it right means bringing a big, brand-new industry to the state, an industry that will spend billions of dollars over the next five years and create upwards of a 1,000 union jobs so that hundreds of wind turbines can be installed, hundreds of miles of electric cable can be laid, and key components of the electric grid – substations and transmission lines back on shore – can be upgraded and built. If New Jersey doesn't get the policy right, then some other state will, and the American offshore wind industry will go there. Over the past five years, the European land-based wind industry has come to America as the market and policy environment have matured. The story will repeat itself soon for offshore wind. It's not a question of *if* – but *when* and *where*.

I'll close by sharing with you an offshore wind success story I came across in a recent issue of the online publication renewable energy world. After the fall of the Berlin Wall, and a draw down in American troop levels in the country, the german port city of Bremerhaven fell on hard times as its services as a supply harbor to the US army were drastically scaled back. It was also at this time that Bremerhaven was losing business to lower-cost Asian and eastern European shipyards. The combined effect was devastating: 3,500 port workers lost their jobs and the city's population shrank by 25 percent.

But Germany's national policies to ensure development of 30,000 megawatts of offshore wind by 2030 and an investment of 250 million euros into the city produced an offshore wind "boomtown." Here are the results:

1. Four new production facilities for turbines up to six megawatts in size;
2. Two manufacturing plants for rotor blades up to 200 feet long;
3. A design and manufacturing facility for offshore steel foundations for offshore wind;
4. Two major R&D centers, containing one of the largest wind tunnels and blade testing facilities in the world;
5. Bachelor- and master-of-science programs in wind energy at the local university; and
6. Last but not least, the creation of 700 new jobs over the last four years and an additional 300 to 500 expected in the near term.

This is the kind of future we can have in New Jersey with the right policies – such as the straw proposal we are discussing – to bring offshore wind to the state.

Thank you for your time and I am happy to take any questions you may have.

IN THE MATTER OF OFF-SHORE WIND SET-ASIDE CHANGES TO THE NEW JERSEY RENEWABLE ENERGY PORTFOLIO STANDARDS (NJRPS) RULES, N.J.A.C. 14:8-2

BPU DOCKET NO. EX08100930

MARCH 26, 2009 PUBLIC COMMENTS BEFORE THE

NEW JERSEY BOARD OF PUBLIC UTILITIES

BY

CLINTON L. PLUMMER, VICE PRESIDENT - DEVELOPMENT

ON BEHALF OF

DEEPWATER WIND, LLC

Good morning President Fox and Members of the Board. My name is Clinton Plummer; I am Vice President of Development at Deepwater Wind, LLC ("Deepwater") and am here today representing Deepwater. As was mentioned previously, Deepwater has partnered with PSEG Renewable Generation to create Garden State Offshore Energy, LLC ("Garden State"), which is exclusively focused on developing offshore wind serving the State of New Jersey. Given our focus on this State, we very much appreciate the opportunity to share with you our comments on the Board Staff's Offshore Wind Renewable Energy Certificate ("OREC") straw proposal.

I would like to start by saying that Deepwater agrees with the New Jersey Energy Master Plan in that "*there is an opportunity for New Jersey to redesign its energy system while establishing a clean energy industry as a major part of our economy*." In fact, the offshore wind project proposed by Garden State would not only deliver up to 350 MW of clean, renewable power to the State, but also would create hundreds of jobs right here in New Jersey. And this is just the beginning. If the State moves quickly, and creates an environment favorable to the

development offshore wind, then New Jersey could benefit from some of the same economic upturns that the German cities of Bremerhaven, Emden and Rostock have enjoyed as a direct result of offshore wind development.

However, as my colleague Robert Gibbs mentioned previously, in order to build an offshore wind farm, a company such as Deepwater must assume considerable regulatory and commercial risk and absorb significant development costs long before there is any certainty of a return. We must invest millions of dollars to simply determine the feasibility of a project. Once a project's feasibility has been established, then we must then invest - and risk - billions of dollars to construct the offshore wind farm.

Deepwater believes that the OREC straw proposal put forth by the BPU can, with a few clarifications, unlock the potential benefits of the development of offshore wind for the State of New Jersey by overcoming a portion of the regulatory and commercial risks I just mentioned. Specifically, there are three components of the OREC straw proposal that we believe are absolutely crucial to the viability of this fledgling industry in New Jersey.

First, we commend the BPU's recommendation to establish a firm price for the first Vintage Year of OREC's no later than 30 days prior to the February 2010 BGS auction. Price certainty will allow companies such as Deepwater to continue to invest the millions necessary for the development of an offshore wind farm because we will know that, if built, a project will be able to earn a certain level of income. As my colleague from PSEG mentioned previously, we believe that it is in the best interests of developers, ratepayers and regulators to have as much information as possible when submitting or assessing the accuracy of price bids. As such, we concur with PSEG's recommendation that for the Vintage Year 2013, the BPU should work with pre-qualified offshore developers, as determined through the straw proposal process, and an

independent consultant of its choosing to establish an OREC price based upon the best available information. For Vintage Year 2014 and thereafter, an RPP will be a reasonable means of establishing an OREC price.

Second, we applaud the BPU's proposed structure of serving as the clearing house for collections from Suppliers and payments to OSW Designated Facilities. This structure will facilitate the lowest possible cost of energy by allowing developers to finance against the creditworthiness of the State.

Third, we agree that a rigorous prequalification of OSW Developers participating in the annual Request for Pricing Proposals will not only maximize the likelihood of the State receiving an Operational Project on schedule, but also minimize the risk of delay caused by artificially low bids submitted by unqualified developers. Deepwater suggests that the initial round be limited to the three pre-qualified bidders and that in successive RPP's, the BPU consider the quantity of content produced in New Jersey as a factor in deciding qualifications.

These three things – price certainty, the BPU's "clearinghouse" approach, and a rigorous prequalification – are aspects of the OREC straw proposal that we believe will contribute significantly to the success of this program. There are, however, three areas in which the OREC straw proposal needs clarification or revision in order to succeed.

First, given that developers will be investing billions of dollars to build the OSW Designated Facilities on the expectation of receiving ORECs as described in the straw proposal, it will be absolutely necessary to provide lenders and other capital partners with some form of surety that the OREC revenues assured to the OSW Designated Facilities will not be compromised in the future. Without such assurance, securing financing for a billion-dollar

project – especially in today's financial environment - will be very difficult. Deepwater would be happy to recommend language based upon prior board proceedings.

Second, as we understand the straw proposal, the BPU and an OSW Designated Facility will agree upon an annual OREC target (expressed in MWH's), the BPU will commit to purchase all OREC's (at a price based upon full revenue requirement) up to the MWH's established by the annual OREC target, and the OSW Designated Facility will reimburse the BPU with the proceeds from the sale of its output in the PJM day ahead market. Given that the OSW Developers must bear production risk, we believe the program will be most successful if the BPU establishes a fair and symmetric means of compensating OSW Designated Facilities. Clearly, if the OSW Designated Facility produces less than the annual OREC target, then it will receive less income. Therefore, we propose that if the OSW Designated Facility produces more than the OREC target, then such facility should be entitled to the proceeds from the sale of the power produced in excess of the annual OREC target.

Third, and further to my previous suggestion, we propose that if an OSW Designated Facility produces more than the annual OREC target, then the OSW Developer should have the option to either (1) sell the excess renewable attributes – independent of the excess energy – in the NJ Class I REC or voluntary markets or (2) hold excess ORECs for up to five (5) years. We believe that five years is necessary because of the annual variation in wind resources.

To reiterate: we believe the OREC straw proposal, with the modifications suggested above, can be successful in moving New Jersey towards the objectives of the Energy Master Plan. We also believe this program will minimize risk to ratepayers because of the competitive process used to set the OREC price, and because ratepayer subsidy will not be required unless

the offshore wind farms are built. We commend the Corzine administration and the BPU in particular, for your vision and leadership in creating this OREC straw proposal.

I very much appreciate your time, President Fox and the Members of the Board, as well as the opportunity to speak with you today. If you have any questions, I would be happy to answer them at this time.

BEFORE THE
NEW JERSEY BOARD OF PUBLIC UTILITIES

NEW JERSEY OFFSHORE WIND
RENEWABLE ENERGY CERTIFICATE PROGRAM

COMMENTS
OF
PEPCO ENERGY SERVICES, INC.

I. INTRODUCTION

On March 10, 2009, the New Jersey Board of Public Utilities ("BPU") issued a "Public Hearing Notice and Opportunity for Comment" in connection with the Revised Straw Proposal: New Jersey's Offshore Wind Renewable Energy Certificate (OREC)" (the "Draft Proposal"). The Draft Proposal was prepared by the BPU Office of Clean Energy ("OCE"). The Draft Proposal summarizes the general framework and business rules for the OREC program outlined in New Jersey's Energy Master Plan.

II. COMMENTS

PES is a competitive supplier of retail electricity to customers in the mid-Atlantic region. PES is a licensed electricity supplier in New Jersey, Connecticut, Pennsylvania, Maryland, Massachusetts, Delaware, District of Columbia, New York, Illinois, Texas, and Virginia. PES actively participates in various working groups in these jurisdictions and has experience working with the different commissions' staffs as they implement various retail choice and environmental regulations, statutes, and requirements.

The Guiding Principles of the OREC proposal state that one of the goals of the Program is to "minimize ratepayer impacts." However, PES is concerned that the Draft Proposal does not minimize ratepayer impacts, but will increase the costs for ratepayers as the proposal introduces new and potentially costly risks to both competitive suppliers and Basic Generation Suppliers ("BGS"), and thus to New Jersey consumers.

PES is also concerned that the current proposal does not address existing contracts that competitive suppliers already have in place that span OREC plan years and that these suppliers will be financially harmed if they cannot pass through their OREC obligations to customers.

PES identifies below issues with the Draft Proposal and suggests changes that address concerns without major structural changes to the proposed program. If implemented, the changes proposed by PES will reduce ratepayer impacts and protect competitive and BGS suppliers from financial harm during the transition from the current rules implementing the Renewable Portfolio Standards ("RPS") to one that includes ORECs.

A. The OREC Requirement should be tied to a Percentage of Load Served as with the Current RPS.

The Draft Proposal changes the calculation of the renewable obligation for both competitive and BGS suppliers (hereinafter referred to as "suppliers") from a percentage of the load served (as is the case with the current RPS rules) to a supplier's percentage of retail electric sales in the State of New Jersey over a plan year, times the number of ORECs for the plan year. This change is problematic because a supplier will not know until well after the completion of the plan year in question the number of ORECs it must procure to meet its obligation. Because the quantity of the obligation is not known, neither is the cost of the ORECs. When preparing pricing offers under the current methodology, a supplier knows the percentage of a customer's load that must be met with specific types of renewables, and it also has a keen understanding of its load under a variety of weather and economic conditions. The supplier can hedge its renewable needs based on this knowledge.

However, under the Draft Proposal, a supplier will not know its share of New Jersey's retail sales until after the plan year is over so it will be impossible to incorporate the cost of ORECs required to meet the supplier's obligation into a retail pricing offer. While some retail contracts may include the ability to pass certain costs through to the customer, not all contracts do, particularly those awarded by State and local government bodies. Furthermore, in some cases, the supplier may no longer be serving a customer when the supplier finds out its actual OREC obligation and cost and may have difficulty collecting these costs retroactively.

To offset this regulatory uncertainty, suppliers, acting rationally, will likely add risk premiums to their pricing which will increase the cost to New Jersey consumers. The impact of this uncertainty can be lessened if the BPU incorporates the following proposal.

PES proposes that the BPU creates a specific percentage of load for which ORECs are required for a five year period. The percentage will be based on the BPU's desired OREC requirement as stated in the current proposal, except that true-ups will not occur. For example if the BPU's objective is to have the marketplace purchase 1,000 ORECs for the first plan year and the expected retail sales for the plan year are 100,000MWH, then each supplier would have a 1% OREC requirement for that year. The 1% requirement is obtained by dividing the 1,000 ORECs for the plan year by the expected retail sales for that year. PES' proposal is for the BPU to establish an OREC percentage for each of the first five plan years in this manner. Near the end of the first plan year the BPU would re-evaluate its OREC requirement for the sixth plan year, along with developing its estimate of retail sales for that year to arrive at the required OREC percentage for the sixth plan year. Through this process, suppliers would always understand their OREC percentage for each of the next five plan years. By removing the uncertainty associated with a supplier's OREC obligation for each of the next five plan year, this proposal will eliminate the need for a supplier to add a risk premium to all pricing, which will reduce the cost to consumers, while allowing the BPU to adjust the percentages so that OREC purchases are made at levels that achieve the goals of the Energy Master Plan.

B. <u>Suppliers Should Have a Limited Exemption from the OREC Requirement for Existing Contracts</u>.

Competitive suppliers operating in New Jersey that have existing contracts that span OREC plan years will be financially harmed if they can not pass through the cost of their new OREC obligations.

PES has two suggestions for dealing with this issue. First, since the longest retail contracts competitive suppliers offer tend to be five years in length, the BPU should set the OREC target or the percentage of OREC requirements if PES's proposal above were adopted, for a five year term instead of the three year term proposed. If a provision such as this is not

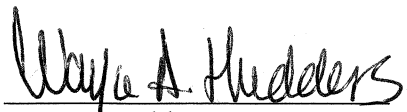
adopted, then suppliers will either stop offering longer term contracts, which are very desirable to customers when energy prices are low or falling, as is currently the case, or they will add additional risk premiums into their prices. PES recognizes that this proposal if adopted would appear to prevent the BPU from starting the OREC program as of June 1, 2013 as planned since 2013 is only three years away from when final OREC regulations are likely to be finalized. Another alternative is for the BPU to maintain the June 1, 2013 implementation target but exempt from the OREC requirement the load that is already under contract until these contracts end. A supplier would be required to be able to demonstrate the basis for the exemption of load from the requirement.

Competitive suppliers and ratepayers would both benefit under this proposal. If suppliers become saddled with potentially unrecoverable costs caused by the creation of the OREC program they will add additional risk premiums into their pricing, particularly for fixed price offers, as the risk of unrecoverable costs will increase. These risks will adversely affect consumers who will bear higher electricity costs and more stringent terms and conditions.

III. CONCLUSION

PES appreciates the opportunity to submit these comments. PES respectfully requests that the BPU accept its recommendations to improve the Draft Proposal.

PEPCO ENERGY SERVICES, INC.

By: 

Wayne Hudders
Senior Energy Market Analyst

March 25, 2009

Filed with NJBPU via email: anne.mcshea@bpu.state.nj.us

New Jersey Offshore Wind : Alaska Prudhoe Bay Crude Oil

Alaska and New Jersey, "perfect together." For over 30 years, Alaskan oil has been a resource that is taxed to benefit the people of Alaska. Each year, the residents of Alaska can expect a dividend or royalty check from revenues generated by the states tax on crude oil production. Whereas Alaskan oil may eventually run dry due to depletion, New Jersey can expect the offshore winds to blow forever. New Jersey can and should develop its offshore winds resource to benefit the residents of the state, both financially and environmentally.

The back of the envelope numbers, based on an article in the UK Guardian newspaper

http://www.guardian.co.uk/environment/2008/nov/04/greater-gabbard-windfarm-sse-npower/print

regarding a 50% stake that changed hands in the North Sea Greater Gabbard 500 MW windfarm are:

A 3000 MW windfarm should cost about $12 billion dollars and return revenues of $25 billion dollars over 20 years. (with the O'RECs priced at $150-$200). The wind will continue to blow after the 20 year O'RECs are retired.

The state of New Jersey has a huge opportunity to offer "green", socially conscious investors and investment funds "green bonds" to fund building the 3000 MW. Revenues accrued during the early stages can go towards funding the buildout of the latter stages of the windfarms. Bondholders can receive payment in kind- additional bonds, in lieu of interest payments until all 3000 MW are completed and in production.

Reasonable development, operations and maintenance fees should be expected.

The state, reluctant to offer new bond issues, should issue bonds for projects that will reduce New Jersey's budget deficit, especially "green projects."

New Jersey should retain ownership of the resource to benefit the citizens of the state for many years to come.

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-----Original Message-----
From: Pfeifferjr@aol.com [mailto:Pfeifferjr@aol.com]
Sent: Tuesday, March 24, 2009 9:14 PM
To: McShea, Anne
Subject: Off-Shore Wind Proposal Comments

Anne,

My only concern with the process for creating special REC's for solar and now off-shore wind is that you inadvertently are reducing the value of regular REC's, such as for on-shore wind. There are new technologies being developed as a result of innovation in the renewable energy market. It is not wrong to give incentives to develop wind off shore, just make sure that there are still sufficient incentives for renewable energy systems that can be applied on land.

One type of technology that I'd like to reference is the proliferation of small wind systems that can be mounted on the tops of apartment buildings, commercial buildings and, in some cases, even on houses. A good REC program should be an equal opportunity incentive, not just an incentive for mega-projects such as the ones proposed for off-shore wind.

Regards,
James Pfeiffer
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