

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service
Commission held in the City of
New York on December 15, 2004

COMMISSIONERS PRESENT:

William M. Flynn, Chairman
Thomas J. Dunleavy
Leonard A. Weiss
Neal N. Galvin

CASE 03-E-0188 - Proceeding on Motion of the Commission Regarding
a Retail Renewable Portfolio Standard.

ORDER AUTHORIZING FAST TRACK
CERTIFICATION AND PROCUREMENT

(Issued and Effective December 16, 2004)

BY THE COMMISSION:

INTRODUCTION

By Order issued September 24, 2004,¹ the Public Service Commission of the State of New York (Commission, PSC) adopted a policy of increasing to at least 25 percent the percentage of electricity used by retail consumers in New York State that is derived from renewable resources. Consistent with this policy, the Commission also adopted a renewable portfolio standard (RPS) program. In this Order, for the initial RPS solicitation only, we adopt on an emergency basis, pursuant to section 202(6) of the State Administrative Procedure Act (SAPA), expedited or "fast-track" measures for facility certification and procurement

¹ Case 03-E-0188, supra, Order Regarding Retail Renewable Portfolio Standard (issued September 24, 2004)(September 24 Order).

solicitation to enable the RPS program to leverage the benefits of federal tax incentives. This action will also help to promote development of the renewable generation industry in New York State.

BACKGROUND

In adopting the RPS program, the Commission, *inter alia*: established two tiers of eligible renewable resources (Main Tier and Customer-sited Tier); set annual, incremental MWh renewable energy targets for the years 2006-2013; required the use of financial incentives to encourage the development and operation of eligible renewable generation facilities; directed the use of a non-bypassable wires charge on certain delivery customers of each of the State's investor-owned utilities to raise the revenue necessary to support the program; and adopted a central procurement model to be administered by the New York State Energy Research and Development Authority (NYSERDA).

The September 24 Order also directed Staff to develop, by March 31, 2005, an implementation plan for PSC approval that would address in more detail the various elements of the RPS program. These matters include, but are not limited to: criteria and procedures to determine facility eligibility; procurement models that may be used by the central procurer for Main Tier and Customer-sited Tier resources; a process to determine the future eligibility of technologies not currently eligible for participation in the RPS; criteria for determining financial eligibility of existing hydroelectric facilities of five megawatts or less, existing direct combustion biomass facilities, and existing wind facilities not currently eligible to participate in the RPS; design of an on-going monitoring and evaluation program; potential modifications to the Environmental Disclosure Program to accommodate the RPS; a mechanism to ensure

the allocation and disclosure of renewable power related to the RPS surcharge to the retail customers paying the RPS surcharge; the process and issues appropriate for the 2009 review of the RPS; and, projected administrative costs.

Notice of proposals pertinent to the full implementation plan was published in the State Register on November 10, 2004. At the time of the issuance of the September 24 Order, we anticipated that NYSERDA's initial procurement solicitation for the 2006 program year would occur in the summer of 2005, which would allow us the first quarter of 2005 to assess the various proposals carefully before approving the full implementation plan. This general approach continues to remain reasonable, and we intend to consider and approve the full implementation plan before the end of March 2005.

The recent enactment of federal law, however, requires that some elements of the implementation plan, namely, facility certification and procurement solicitation, be decided, at least for the initial procurement, on an expedited basis to take advantage of this opportunity to save New York ratepayers tens of millions of dollars. In particular, this Order addresses facility certification processes and procurement models for Main Tier resources that are most suitable under the specific market conditions resulting from the one-year extension of the federal Renewable Electricity Production Credit (also known as the Production Tax Credit or PTC).²

For projects that qualify, the PTC provides a ten-year stream of tax credits estimated at approximately 1.8¢/kWh for wind and closed-loop biomass³ and a five-year stream of tax

² 108 P.L. 357, 118 Stat. 1418, H.R. 4520, 108th Cong. (2004).

³ Closed-loop biomass is any organic material from a plant is grown exclusively as fuel to produce electricity.

credits estimated at approximately 0.9¢/kWh for open-loop biomass,⁴ landfill gas, solar and some other technologies. Several RPS-eligible resources (such as wind, closed-and-open-looped biomass, solar energy, and landfill gas) are eligible PTC resources.

Cost minimization is a primary RPS implementation objective. The current availability of the PTC offers an opportunity to further this objective through the leveraging of the PTC value to the benefit of New York ratepayers. The value of PTC leveraging can be substantial. For example, if approximately 80 percent of the 2006 RPS megawatt hour (MWh) target were to be procured from PTC-eligible facilities, the net present value of the PTC could be as high as \$97 million (assuming a 10% discount rate).

The PTC is currently scheduled to expire on December 31, 2005; that is, a project must be placed in service by this date to qualify for this federal tax credit.⁵ The limited one-year extension of the PTC creates the risk of a lost opportunity to reduce substantially the cost of the RPS to New York's ratepayers.⁶ Therefore, we are establishing, for the program's initial solicitation only, expedited or fast-track

⁴ Open-loop biomass is any organic material, other than closed-loop biomass, that can be used in the production of electricity.

⁵ While Congress has extended the PTC in the past, Congress has also allowed it to lapse and then reauthorized it at a later date.

⁶ In the RPS Cost Analysis (Appendix D to the September 24 Order), the PTC was assumed to be available for the duration of the RPS and its value was estimated to be significant.

facility certification and procurement solicitation processes to allow execution of contracts with sufficient lead-time to capture the benefit of substantial PTC leverage for New York ratepayers. We are also authorizing new Main Tier facilities using resources such as hydro that are not eligible for the PTC to participate in the initial solicitation, provided that they are operational no later than December 31, 2005 in order to receive RPS support.

Notice of this proposed action was published in the State Register on November 10, 2004. The notice explained that comments were requested as soon as possible because the Commission was considering immediate adoption of the proposal on an emergency basis pursuant to §202(6) of the State Administrative Procedure Act (SAPA). To date, comments have been received from the Independent Power Producers of New York, Inc. (IPPNY); the American Wind Energy Association (AWEA); Noble Environmental Power, LLC (Noble); Flat Rock Windpower LLC (Flat Rock); the Joint Utilities;⁷ Airtricity, Inc. (Airtricity); and Multiple Intervenors (MI). SAPA provides an opportunity for public comment subsequent to adoption of an emergency measure and prior to its permanent adoption (SAPA §202(6)(b)).

ACTION PROPOSED IN NOTICE

Facility Certification

As a part of the design of the on-going, long-term RPS program, the Commission may consider, in a subsequent order addressing the implementation plan discussed above, whether we

⁷ Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation comprise the Joint Utilities.

should impose a requirement that all potential renewable energy projects obtain provisional or operational certification by NYSERDA as a pre-condition for participating in an authorized central procurement solicitation (projects that are not so certified would not be eligible to participate).⁸ Under this approach, provisional certification would be necessary for facilities that are not yet constructed. Operational certification would be required for facilities that are constructed and operating at the time of the procurement and for provisionally certified facilities prior to RPS payments.

To take advantage of the market conditions resulting from the PTC, however, the notice proposed that NYSERDA use a streamlined certification procedure, whereby a generation provider would self-certify eligibility based on the criteria set forth in the September 24 Order. Operational certification upon commercial operation (renewed periodically, perhaps once every two years, to ensure that a facility continues to meet RPS eligibility requirements) would be required before incentives are paid. In addition, the notice sought comment on whether we should allow new Main Tier RPS facilities to participate even if they are not eligible for PTC credits.

The notice proposed assigning to NYSERDA the task of developing the appropriate forms and procedures for self-certification, with NYSERDA making initial determinations of

⁸ Alternatively, some states use an optional "advisory ruling" process in advance of solicitations, which allows developers whose projects are still in the development stage to assess the likelihood and conditions under which the project would qualify for RPS support. Other states require provisional certification only for a project that has been selected or that is a finalist for selection.

eligibility.⁹ Under this model, the Commission would hear any appeals of NYSERDA's decisions.

Procurement Models

Objectives

The notice sought comments on the following objectives pertinent to the design of any RPS procurement method:

- Minimize cost to end use customers;
- Contract with projects that have good probability of becoming operational;
- Support project financing;
- Maximize leverage of the program by considering other factors such as the Federal PTC;
- Achieve RPS quantity objectives;
- Minimize interference with competitive wholesale markets;
- Capture economic development opportunities;
- Encourage viable competitive renewable energy and green power markets;
- Create a base of information and experience to facilitate transition to more market based procurement approaches; and
- Create a foundation for future flexibility and process evolution.

Methods

The notice proposed authorizing NYSERDA to use its discretion in choosing among the following three options as the most advantageous expedited procurement process:

⁹ In addition, the forms would advise generation providers that they would be able to identify information that they believe should be treated confidentially during provisional certification pursuant to New York Public Officers Law § 87(2)(d), 21 NYCRR Part 501, and 16 NYCRR Part 6.

1. Auction format;
2. Request for Proposals (RFP); and
3. Standard offer.

The notice sought comments on not prescribing a specific method so as to allow NYSERDA the ability to adapt its procurement solicitation to changing market conditions. The notice provided descriptions of each of the three proposed procurement approaches:

1. Auctions

Auctions work well in circumstances in which the good or service is sufficiently defined such that the winner can be determined solely by its price and not by other factors such as quality or dependability. In certain markets, for example, energy is transacted on the basis of hourly (or other) auctions. In addition, provider of last resort (POLR) service may be acquired through auctions that are held periodically, as may be required (e.g., New Jersey Basic Generation Service). In both instances, the auction procurement targets are fixed; delivery is not in question once the bidders qualify (they are licensed and creditworthy); the contracts are standard; and, the winning bids are unambiguous. Moreover, unless the bidder has violated some pertinent rule (such as bid collusion), the winners are appropriately paid for what they deliver.

Auctions can be structured such that the winning bidders can be paid the same price - known as a clearing or uniform price - or paid what they bid. The choice may depend upon the specific details of the auction and the type of auction utilized; conversely, the choice may also influence the selection of a specific auction model. Ascending-bid auctions, descending-bid auctions, and multiple unit auctions are three such models.

Factors to consider in assessing the potential effectiveness of an auction approach in a particular environment include:

- Are there sufficient numbers of bidders to make the auction competitive?
- Are the commodities offered by bidders equally valued by the central procurer?
- Is there potential for one or a few bidders to dominate the auction?
- Is there opportunity for collusion among the bidders?
- Are there barriers to entry in the auction?

2. Request for Proposals (RFP)

The RFP approach seems to be well suited to situations where multiple objectives are to be considered and weighed. This is typically the case where factors other than price are crucial, where the commodity is not uniform, where there is development or quantity risk, where there is flexibility on the amount to be procured, and/or where some negotiation with the highest-ranking bidder is contemplated. Note that "pay-as-bid" is typically a component of the RFP approach.

RFPs are also adaptable to situations where there is substantial variability in the projects offered. For example, when different terms and conditions are in order, location-based effects are relevant, operating characteristics for competing technologies are quite different, project and technology risks are unique, and developer experience is important, the RFP approach may be the most applicable/effective.

In the energy business, RFPs have been widely used by utilities that have sought power from a mix of resources, or from resources with different fuels or pricing structures (so as to create a hedged portfolio, for instance), or with respect to contracting with independent power producers (including Public

Utilities Regulatory Policies Act of 1978 (PURPA) Qualifying Facilities) for power from facilities that were, at the time, not yet in service. RFPs were also used extensively in the divestiture of generating assets during the implementation of restructuring. In general, those transactions that are longer term or more complex are less amenable to a pure price auction and more amenable to RFP or competitive negotiation formats.

Factors to evaluate in this regard include:

- The extent to which non-price considerations are to be explicit criteria in evaluating proposals (including, but not limited to, project type, resource diversity, locational diversity.);
- The extent to which alternative or non-standard contract terms and conditions are to be considered;
- The extent to which project specific due diligence will be required as part of the bid evaluation to obtain assurance on project viability; and
- The frequency with which solicitations are expected to occur.

3. Standard Offers

A standard offer approach provides eligible participants the opportunity to take a contract at a pre-specified price, quantity and duration. Consistent with that year's procurement needs, projects meeting established threshold requirements would be eligible to obtain the stated price, terms and conditions. In essence, the standard offer approach is a simple auction format, with the clearing price administratively set in advance.

The advantage of a standard offer is that it is simpler to administer and less risky for the project applicant than auctions or RFP formats. Establishing a standard set of terms and conditions that is suitable for most participants and establishing a basis for administratively setting the price

level are among the challenges posed by the standard offer format.

Standard offers have been used in a number of contexts. In the power industry, standard offer contracts have been used historically for small qualifying facility contracts under PURPA. A standard offer is also analogous to any number of coupon or rebate programs, with a fixed price or rebate offered to a large number of buyers.

Pricing

Regardless of the procurement option chosen, we authorized NYSERDA in the September 24 Order to provide a financial incentive to renewable generation providers in the form of a premium payment based on energy provided on the condition that, in exchange for this payment, NYSERDA would obtain control of the associated renewable energy attributes and the generation provider would be precluded from selling the attributes associated with that energy. Such a structure (or some similar form) is intended to ensure that New York State ratepayers obtain an identifiable result from the RPS surcharge on their electric bills.

PARTIES' COMMENTS

IPPNY

Focusing primarily on pricing issues, IPPNY urges the Commission not to authorize the Contract for Differences (CFD) approach.¹⁰ It argues that the CFD approach ignores the basic tenet of the New York market design that values energy when and where it is needed most. IPPNY explains that renewable

¹⁰ Although there are variations, a simple CFD in this context would involve NYSERDA paying the difference between the spot market price obtained by a generation provider and an agreed-upon price between the generation provider and NYSERDA.

resources that have their generation determined by natural forces, such as wind, would have no economic interest in following market price signals because these generators would receive their full payment regardless of the level of the market clearing price. In addition, with the CFD approach, generators would have no incentive to schedule maintenance of their facilities at times that maximize the underlying value of energy to the State. IPPNY also claims that the impacts on system operational dispatch would be significant. It further asserts that use of the CFD approach would harm the efficiency and competitiveness of the electricity markets because it could lead to uneconomical decisions with respect to selection of renewable resources, thereby promoting the construction and operation of unnecessarily costly renewable resources.

IPPNY acknowledges that it may be possible to use a more complicated variation of the CFD approach by attempting to determine the premiums that are implicit in each of the total price bids and to rank the bids based upon minimizing the premium. It notes that this would require NYSERDA to estimate future wholesale market revenues that would apply to each bidder for the duration of its contract. It perceives a problem with this because NYSERDA, in addition to estimating wholesale energy costs in general, would also have to estimate the amount of energy each bidding renewable resource would deliver at different times of the year and at different times of the day as well as the value of the energy at the times the resources are delivering the energy. NYSERDA would be required, moreover, to estimate the amount of installed capacity that each renewable resource would provide and the value of that capacity.

IPPNY warns that having NYSERDA make these estimates with the CFD approach becomes even more complicated and prone to error in the case of out-of-state renewable resources.

According to IPPNY, since out-of-state resources can sell their energy in their home states or provinces at the time it is produced and have the balance of the calendar month to deliver an equivalent amount of energy to New York, implementing the CFD approach will require defining the energy value that would be deducted to determine the "difference" that would be paid by NYSERDA. In the case of imports, IPPNY states, it would be difficult to define the difference because the delivery period would be independent of the time at which the energy is generated. In addition, it would also be difficult to determine the "difference" associated with imports because the NYISO does not estimate a price for the resources' location.

In contrast to the CFD approach, which IPPNY states would require NYSERDA to take all the risk for forecasting errors and would reward inefficiency, IPPNY prefers a fixed price approach because it results in awards to the most efficient developers and ensures that resources are sited in the best locations. According to IPPNY, NYSERDA has the expertise in place to evaluate fixed price bids. The fixed price approach would select suppliers with the lowest bids, ensuring that bidders take the risk for any errors or misrepresentations of their projects and that all bidders are evaluated on a fair and competitive basis.

IPPNY also argues that a Commission delegation of the bid evaluation process to NYSERDA, without clear guidance from the Commission to inform the evaluation process, would amount to an improper delegation of the Commission's jurisdiction to review and approve the rates and charges to the State's retail electric ratepayers. It asserts that, in contrast to the system benefits charge (SBC) evaluation process, the Commission appears to be contemplating an open-ended process that would allow NYSERDA too much discretion in making decisions that may have an

impact on retail rates. This situation becomes especially acute, it states, if NYSERDA were to use the CFD approach.

AWEA

AWEA agrees that the Commission should move quickly to take advantage of the extension of the PTC. It urges the Commission to allow all RPS-eligible resources to bid in this fast-track procurement process regardless of whether or not they are eligible for the PTC. AWEA explains that signing up resources as early as possible, not only for this initial procurement solicitation but for subsequent procurement solicitations as well, would help ensure success of the RPS program because developers need a significant amount of time to bring a project to operation.

AWEA advises that only projects that can reasonably be expected to enter operation on schedule should be awarded contracts. It states that self-certification and provisional certification are acceptable for the expedited procurement. It requests that the Commission and NYSERDA should prepare a list of certification requirements to be used as guidance for self-certification. As examples of such criteria, AWEA mentions requiring approval of the project's System Reliability Impact Study from the New York Independent System Operator, Inc. (NYISO) and possession of permits and approvals (environmental and local) or expectation of issuance by a specific date.

AWEA also urges the Commission to direct NYSERDA to impose a bid fee or bond requirement (perhaps on a MW or expected MWh basis) on projects participating in procurements. It explains that the requirement to post security, which can be forfeited or used to pay damages as described in contract language, would help ensure that only projects with every expectation of successful development and operation would bid into the process. A portion of this security, it suggests,

should be forfeited in the event certain milestones, such as obtaining permits and approvals, are not met.

Regarding the procurement method, AWEA suggests that each of the proposed methods (auction, RFP, and standard offer) have both benefits and detriments. It asserts that a well-designed auction would provide the most sufficient and transparent approach, but that given the time constraints there may be impediments to using an auction for the expedited solicitation.

Regarding pricing options, AWEA notes that contracts can be awarded with payments made on an as-bid basis at market-clearing prices, or using a CFD where the premium paid by NYSERDA would fluctuate depending upon energy prices (and a CFD can, in turn, be awarded on an as-bid or market-clearing basis). It suggests that the option chosen would have a direct influence on the market behavior of bidders and on the cost of the program. For example, according to AWEA, the use of CFD means bids are based on the total price needed by the project, and the premiums paid represent the difference between the total price and the price of the energy sold. AWEA asserts that this approach approximates most closely the standard power purchase agreements used widely in the wind industry. It notes that contracts based on the total price (for energy and environmental attributes) have less risk for developers, which makes project financing less costly, resulting in lower price bids and a lower cost RPS program. In addition, AWEA states that while payments on an as-bid basis are generally used for RFP's, the energy market uses market-clearing prices, and this approach should be considered.

Noble

Noble agrees that the Commission should adopt, on an expedited basis, measures that would take advantage of the PTC

extension. It argues that, to satisfy the goal of obtaining renewable energy quickly, all RPS-eligible facilities should be able to participate, even though they may not be eligible for the PTC. To avoid the awarding of contracts to projects that are unlikely to become operational by the end of 2005, Noble argues that bidders should be required to submit information demonstrating their likelihood of being permitted, financed, constructed, and in commercial operation before the end of 2005. It proposes a requirement that bidders be required to provide a "substantial" fee ranging between \$25,000 and \$50,000, which would be refunded to non-winning bidders. Noble also suggests that the Commission require bidders to demonstrate financial resources sufficient to complete development and construction of the project and the successful bidders to meet certain milestones in order to keep the projects on track for the PTC deadline.

Regarding procurement models, Noble explains that, because of the tight timeframe, the standard offer approach may be most suitable for this initial solicitation. It states that in this initial solicitation, where an expiring tax credit is the major reason for a speedy process, a standard offer is likely to yield the easiest and quickest evaluation process. In contrast, according to Noble, evaluation of varying responses to an RFP would take far more time to analyze.

Flat Rock

Flat Rock supports the use of an expedited procurement process, with contracts awarded within the first four weeks of 2005. It believes that this approach would reduce the cost of the RPS program, facilitate achieving the RPS goals for 2006 and beyond, and accelerate economic benefits from the RPS to local communities. It warns, however, that the procurement process must be carefully designed so that only credible facilities

participate, the contract terms provide a basis for financing, and protections are included so that overly high prices are not paid. To achieve these ends, Flat Rock urges that the Commission require a letter of credit or bond requirement on projects participating in the procurement process. It suggests a bond requirement of \$2,500 per megawatt of installed capacity, which, it states, is the same bonding amount imposed by the Pennsylvania Sustainable Development Fund in an October 10, 2002 wind energy solicitation, as appropriate for this program as well. According to Flat Rock, this level would be high enough so as to discourage bids from developers that are not likely to proceed with development in 2005, but not so high as to discourage bids from credible developers that may not be as highly capitalized as other participants.

Flat Rock supports all three of the procurement options discussed in the notice as long as the procurement process can be initiated in 2004 and conclude with signed contracts no later than January 31, 2005. Flat Rock recognizes that the initial solicitation might include methods and processes that differ in later solicitations, but it argues that it is critical that the initial step should develop credibility with the public, the industry, and participants. It explains that, if a standard offer is the chosen procurement method, the price should be based on the recommendation of experts who should take into account the recent increases in the cost of wind power and green attributes values in other areas. It asserts that, if the auction option is chosen, transparent competition among a sufficient number of multiple bidders would probably suffice. Finally, if an RFP format is the procurement mechanism, Flat Rock recommends that acceptance of qualified proposals should be based on as few and as transparent criteria as possible (preferably, price alone).

Flat Rock also stresses the importance of the procurement contract, explaining that, unless the contract can be used as a basis for financing, it is doubtful that any project would bid. It suggests vetting the proposed contract with the industry by placing the proposed draft contract on NYSERDA's Web site with an invitation to comment. It also notes that the contract and bidding process should be as simple and transparent as possible.

Based on its analysis and experience, Flat Rock suggests various terms that should be included in the procurement contract. In addition to the bond parameters mentioned above, it suggests that: the bond should provide that a facility installing fewer megawatts than proposed in its bid would constitute a call on the bond; the contract term must be for a minimum of ten years because, in its view, this is the period necessary for project financing; to ensure simplicity and uniformity of bids, all developers should be asked to present a price for the same term; for the purposes of simplicity, each project should provide only one bid; and, the contract should also make clear that after expiration of the contract period the facility would be free to sell its energy and attributes to other parties.

Regarding price, Flat Rock urges that projects should be bid and selected based on a flat rate. It notes that while future procurements may explore the benefits of bids containing fixed or variable escalating or declining rates, for the initial procurement, flat rate bids would probably be the most transparent and easiest to evaluate. Flat Rock further explains that a developer's bid should be for a set dollar amount per MWh for an estimated number of MWhs per year or fraction thereof, if only a portion of the facility's output is bid into the RPS procurement. It states that there should be no penalty if the

facility does not meet this estimated annual energy production and that the contract should also provide assurance that NYSERDA will purchase the rights to renewable attributes related to energy in excess of that estimate.

According to Flat Rock, this assurance is crucial because, due to the way the RPS is designed, there is no market for renewable energy credits to use to adjust to a specifically defined contract amount. That is, the project cannot buy renewable energy credits (RECs) in order to keep its commitment to NYSERDA when the project itself under produces and/or sell RECs from overproduction to other purchasers. It argues, therefore, that the contract should be defined in terms of a goal and NYSERDA should commit to purchase the project output whether this is over or under the goal.

Flat Rock further urges that NYSERDA's credit rating should be Baa3 (Moody's) or BBB -(Standard & Poors) or higher and that if NYSERDA's credit rating falls below the standard, the contract should require NYSERDA to post an additional two years of revenue as security of the contract. Flat Rock also states that the contract should provide that it is assignable by either party upon written consent of the other party and consent will not be unreasonably withheld. It also states that the contract must provide that the developer may grant a security interest in the contract without approval of NYSERDA. This, Flat Rock claims, is a critical provision for obtaining project financing based on the contract.

Joint Utilities

The Joint Utilities support efforts to move forward expeditiously but warn that a potential for unintended or undesirable consequences may arise if the process is not appropriately designed or implemented. The Joint Utilities urge adoption of a process that can be used both in the initial

solicitation and in future solicitations so that potential bidders will gain information that can be used in shaping their participation in the RPS program. The Commission should also make it as clear as possible, the Joint Utilities further advise, that the solicitation method adopted for the initial procurement will not set a precedent for the future. Regarding procurement methods, the Joint Utilities believe that the descending clock auction approach results in more cost efficient prices than any other approach.

Airtricity

Airtricity supports establishing an expedited procurement process to capture the potential financial advantages of the PTC. Airtricity believes that both the standard offer approach and the auction approach are superior to the RFP approach. It recognizes, however, that due to the time constraints involved here, the Commission may choose the RFP approach. Airtricity states that, based upon its experience, it is concerned that successful bidders may not actually construct their projects because, in an effort to be selected, they may bid too low to be financially viable.

To address this issue, Airtricity suggests that the following items be required in any bid submission by a wind developer: (1) a minimum of 12 months of wind data reviewed by an independent expert; (2) a demonstration that the developer has actual control of the land on which the project is proposed to be sited; and (3) a completed initial grid interconnection study. It argues that these requirements are not overly burdensome, but will winnow out the potential bidders who are unlikely to be in a position to take advantage of the PTC by becoming commercially operational by December 31, 2005.

To help obtain financing, Airtricity believes that the Commission should establish a floor price for RPS payments under

the expedited procurement process of four to five cents per kilowatt hour. It asserts that a reasonable floor price would decrease fiscal uncertainty and facilitate participation by more renewable developers. It maintains that more renewable developers would participate because a floor price would reduce the probability that a few large developers with access to substantial capital resources would control the market. A floor price would also discourage unrealistically low bids that could undermine the development of a robust long-term sustainable RPS market in New York. Finally, Airtricity notes that the RPS payments must remain available for a reasonable period of time, which it believes would require a minimum contract period of 12 years.

MI

MI recommends use of the RFP approach and a cost-based pricing methodology for the initial procurement. It explains that, because the RPS is a subsidized program paid for by ratepayers, each subsidy should be limited to the minimum amount necessary for a particular project to be built. According to MI, NYSERDA should issue an RFP that requires each generation provider to provide specific cost information about the renewable facility, including capital costs, operation and maintenance costs, and a proposed rate of return on equity. The information should also include the anticipated capacity factor for the facility and the revenue per kilowatt hour required to construct and operate the plant.

MI states that selected resources should receive a subsidy based on a CFD to minimize RPS costs and recommends against use of a fixed price or standard offer. Under MI's approach, each CFD would be based on the costs of development of a specific project and any revenues received by that project in excess of the amount needed to cover the project's cost of

service and a reasonable rate of return on equity would be returned to NYSERDA. MI defines the subsidy as the difference between the payments received by the facility from the NYISO (or other buyers) for energy, capacity, and ancillary services, and the facility's cost of service. Under the MI proposal, whenever NYISO payments exceed the subsidized price on an annual basis, the project would refund the credit to the RPS program. MI states that this approach would ensure that developers do not receive a windfall at the expense of New York consumers. MI also states that a CFD approach would shift risk to consumers, and therefore, a project's cost of debt and cost of equity should be less than if another approach is used; it asserts that the CFD approach is the only way to avoid overpayments to generators.

MI argues against participation of Main Tier facilities that are not eligible for the PTC in the initial solicitation. MI asserts that allowing these resources to participate would increase the cost of the RPS program because renewable resources will become less expensive over the next ten years. MI also urges the Commission to state that the initial procurement procedures would not establish precedents for future RPS procurements.

DISCUSSION

None of the parties that submitted comments objected to the Commission acting expeditiously to take advantage of the availability of the PTC. Guided by the comments and further analysis, and for the reasons discussed below, we will authorize NYSERDA, for the initial solicitation, to develop a self-certification process, with appropriate forms and subsequent verification, and to use an RFP procurement process with a fixed price bid and guarantees, including, but not limited to, letter-of-credit, bid deposit, and milestones.

Facility Certification

The certification procedure for both the initial solicitation and the long-term RPS program should be developed with these objectives in mind:

- Provide certainty to generation providers to minimize pre-development cost and risk due to uncertainty in potential eligibility;
- Minimize administrative burdens to generation providers and regulators;
- Minimize time requirements so as not to unduly slow the procurement process;
- Ensure that only eligible projects are certified;
- Create an open and transparent process; and
- Afford confidentiality to generation providers during the development process.

Parties generally agree with the proposal for the initial solicitation that allows generation providers to self-certify facilities' RPS eligibility in bid papers. In addition to this, we will require that a project obtain operational certification regarding eligibility upon commencement of commercial operation before production incentives would be paid. We will also authorize NYSERDA to require periodic renewal of operational certification and notification to NYSERDA of any material change to avoid disqualification.

We agree with AWEA, Noble, Flat Rock, and Airtricity that the RFP and contracts should include conditions that are designed to ensure that only generation providers that are serious about bringing their projects to commercial operation on a timely basis – and the probability of doing so – should be awarded contracts. Requiring a bid deposit with submission of the bid and letter of credit as a condition of a contract award is certainly a reasonable way to accomplish this objective. The amounts contained in both financial instruments should be set at

a level sufficient to discourage bidding by generation providers that have little or no probability of their projects being placed in service by December 31, 2005; however, the amounts should not be so high as to be onerous, especially for small projects.

Regarding milestones, it may be impractical for this initial solicitation (because of the tight time frame) to require that a project must have obtained NYISO approval of its System Reliability Impact Study or have fully completed the environmental review process in order for a contract to be offered. Instead, conditions similar to those suggested by the commentators designed to give NYSERDA confidence that a project would have a high likelihood of achieving certain milestones during the year should be considered by NYSERDA. For instance, NYSERDA could require submission or proof of completion or receipt of: a plan and timeline for project milestones; site control; a resource or fuel assessment; a financing plan; acceptance by the NYISO and/or the delivery utility (as appropriate) of an interconnection application and scope of work for any needed interconnection study, with a date in the queue that is prior to December 31, 2005; and all permits and approvals or evidence that all permits and approvals are highly likely to be secured in time for the project to be commercially operational by December 31, 2005.

Another contract condition NYSERDA could consider is an agreement that failure to satisfy these requirements could result in loss of some or the entire amount of the security. In cases where a marketer or broker or some entity other than the facility owner submits the bid, it would be appropriate for NYSERDA to require the bidder to demonstrate that the bidder would have contractual control of the energy output of the facility.

Participation of Non-PTC Eligible Projects

Only MI disagreed with the proposal to allow all RPS-eligible projects to participate in this initial solicitation, even though the impetus for the fast-track solicitation is to take advantage of the PTC extension. MI's concern, that allowing these projects to participate would result in high RPS program costs because renewable projects will become less expensive over time, is misplaced. The September 24 Order established annual MWh targets; we expect NYSERDA to conduct procurement solicitations and award contracts with those targets in mind. Exclusion of resources from bidding would not reduce annual targets. Allowing more bidders promotes healthy competition, which puts downward pressure on price to the advantage of ratepayers, and also makes it more likely that first year renewable targets are reached.

To ensure that all bids are fairly evaluated on a compatible basis, non-PTC projects must also demonstrate substantial likelihood of being placed in service by December 31, 2005.¹¹ Projects unable to meet that time constraint may participate in subsequent procurement rounds.¹²

¹¹ Although facilities must meet the December 31, 2005 deadline for placement in service, projects need not deliver energy pursuant to the RPS program beginning January 1, 2006 in order to be awarded a ten-year contract. For example, a project might choose to sell into the voluntary green market for two years and then begin taking RPS payments beginning on January 1, 2008 and continuing through December 31, 2016.

¹² We expect NYSERDA to fill the balance of RPS program goals by conducting one or more "regular" procurement solicitations in the summer of 2005 for projects that would become operational in 2006 and 2007.

Procurement Method

As many commentators suggest, each of the three proposed procurement methods – auction, RFP, and standard offer – that we proposed are valid mechanisms to satisfy the long-term goals of the RPS program. Despite the numerous benefits of the auction method, we determine that this approach is not appropriate for the initial solicitation because to do it well requires more time than is available. Given the time constraint, the simplicity of the standard offer method is attractive. A standard offer, however, must contain a specific price, quantity, and term to be effective. Without information gained through having conducted previous solicitations, determining a reasonable level for these factors, from the perspective of ratepayers and of generation providers, poses serious difficulties.

We will, therefore, direct NYSERDA to use an RFP approach for this initial procurement solicitation. Although this approach is well suited to situations involving many factors and a variety of project characteristics, we believe it can be tailored to focus on one or two variables only, such as price and term. In evaluating bids, appropriate consideration should be given to economic benefits to New York resulting from projects.

Pricing

Another critical consideration in procurement and contracting is the form of product pricing employed. The notice proposed the following pricing options:

- Fixed single price for entire term;
- Schedule/preset but varied prices over term;
- Indexed pricing; and
- Contracts for difference (CFD), with variations.

Any consideration of a particular price structure should include an assessment of its impact on market behaviors. It may be possible that a particular pricing structure found to be favorable to the financial community (CFD, for instance) could cause unintended negative consequences, as IPPNY warns, when used in the markets administered by the NYISO. Such circumstances must be considered in any evaluation of product pricing and procurement model.¹³

We will continue to explore, but decide against adoption of the CFD approach for the initial solicitation. As IPPNY suggests, considerable attention must be given to its design to avoid negative impacts on the energy markets and this analysis would require additional time that could increase risks of higher costs to the RPS program, due to failure to take advantage of the PTC. For this fast-track procurement solicitation, therefore, we will require NYSERDA to seek bids for a term of ten years or less with a constant price per MWh.¹⁴ While we would expect NYSERDA to contract for the rights to the renewable attributes associated with all of the output offered

¹³ Flat Rock stated that NYSERDA must have a certain bond rating to satisfy potential lenders that payments from NYSERDA would be forthcoming for the life of the contract. We disagree. We believe that Ordering Clause 7 of the September 24 Order and the related orders that will be issued pursuant to that clause, as well as the terms of contracts that will be executed between NYSERDA and each utility pursuant to Ordering Clause 6, will render moot this concern.

¹⁴ We reject Airtricity's suggestion that we establish a floor price for the same reason we have rejected the standard offer approach for procurement. We do not have enough information about the market to determine with sufficient accuracy a reasonable floor price.

by a successful bidder,¹⁵ we recognize that in some circumstances it may be prudent to contract for a lesser amount. We will also authorize NYSERDA to reserve the right to reject any and all bids should the pricing or other bid elements not be deemed acceptable.¹⁶

IPPNY's claim that allowing NYSERDA to make final decisions on awarding of contracts would constitute a violation of the Public Service Law has no merit for several reasons. First, it is not a delegation of authority because NYSERDA is a separate state entity with its own established authority to carry out state purposes.¹⁷ Second, the Commission determined the level of the RPS surcharge in the September 24 Order to be just and reasonable. Third, in this Order, we adopt specific criteria for NYSERDA's exercise of its authority as a central procurement administrator; the criteria provide specific guidance for the bid evaluation process.

Emergency Action Under SAPA

Immediate approval of facility certification and procurement solicitation methods would allow the RPS program to

¹⁵ A bidder may decide to reserve a portion of the generation of a facility to satisfy Executive Order 111 or sell into the voluntary green market.

¹⁶ We agree with MI that cost minimization is an important objective; however, the model it proposes is impractical. Its method, use of a cost-based pricing methodology in lieu of market-based approaches, would require conducting a detailed financial analysis of each renewable project, potentially numbering in the dozens and including out-of-state companies. The time delays associated with such analyses would result in the awarding of contracts too late for many projects to achieve the December 31, 2005 deadline. In addition, a cost-based approach is antithetical to the development of competitive markets.

¹⁷ Public Authorities Law §§1850-a, 1851(10), and 1855(17).

take advantage of the extension of the PTC, so that the program (and, therefore, ratepayers) can realize savings estimated at up to \$97 million. This ability to contract with renewable energy providers in time to take advantage of the opportunity offered by the one-year extension of the PTC would be lost if the normally-applicable notice and comment procedure were followed. Moreover, allowing non-PTC bidders to participate in this initial procurement solicitation promotes healthy competition, which puts downward pressure on price to the advantage of ratepayers.

To avoid loss of these tax savings, and to preserve their benefit for the State's ratepayers, we find, as required by SAPA §202(6), that, as suggested in the November 10, 2004 SAPA Notice, immediate approval is necessary for the preservation of the general welfare and compliance with the prior notice and comment requirements of SAPA §202(1) would be contrary to the public interest.

CONCLUSION

It is the Commission's understanding that for developers to close financing and order equipment with sufficient lead-time to meet the PTC deadline, contract awards should be made by no later than the end of January 2005. Accordingly, to capture the opportunity offered by extension of the PTC, thereby furthering our stated objective of minimizing costs to ratepayers, the Commission is adopting measures for this initial solicitation only (facility self-certification, subject to later verification; RFP with a term of ten years or less and a constant fixed price per MWh; security; milestones) that would allow NYSERDA to prepare and issue a competitive solicitation on a timeline that would lead to project selection and contract execution by the end of January 2005.

The Commission orders:

1. New York State Energy Research and Development Authority (NYSERDA) is authorized to develop facility self-certification procedures and forms as described in the body of this Order for use in the initial renewable portfolio standard (RPS) procurement solicitation.

2. NYSERDA is authorized to use a Request For Proposal procurement method containing security guarantees, milestones, contract duration, and a constant fixed price per megawatt hour factor as discussed in the body of this Order in the initial RPS procurement solicitation according to a schedule and in a manner designed to allow it to award and execute contracts at a reasonable cost no later than the end of January 2005.

3. This action is taken on an emergency basis pursuant to Section 202(6) of the State Administrative Procedure Act for the reasons noted in the body of this Order.

4. This proceeding is continued.

By the Commission,

(SIGNED)

JACLYN A. BRILLING
Secretary