STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Application of Champlain Hudson Power Express, Inc. for a Certificate of Environmental Compatibility and Public Need Pursuant to Article VII of the PSL for the Construction, Operation and Maintenance of a High Voltage Direct Current Circuit from the Canadian Border to New York City

Case 10-T-0139

REPLY BRIEF OF INDEPENDENT POWER PRODUCERS OF NEW YORK, INC. IN OPPOSITION TO JOINT PROPOSAL AND ARTICLE VII APPLICATION OF CHAMPLAIN HUDSON POWER EXPRESS, INC.

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A. INTRODUCTION AND GENERAL CONSIDERATIONS

Pursuant to Administrative Law Judges ("ALJs") Kevin J. Casutto's and Michelle L. Phillips' May 8, 2012 Ruling Establishing Schedule and Hearing Procedures in the above-captioned proceeding,[1] Independent Power Producers of New York ("IPPNY"), by its counsel, Read and Laniado, LLP, hereby submits this reply brief in further opposition to the issuance by the New York State Public Service Commission ("Commission") of a certificate of environmental compatibility and public need ("Certificate"), pursuant to Article VII of the New York Public Service Law ("PSL"), to Champlain Hudson Power Express, Inc. ("CHPE") and CHPE Properties, Inc. ("CHPE Properties," and together with CHPE, the "Applicants") based on

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[1] Case 10-T-0139, *Application of Champlain Hudson Power Express, Inc. and CHPE Properties, Inc. for a Certificate of Environmental Compatibility and Public Need Pursuant to Article VII of the PSL for the Construction, Operation and Maintenance of a High Voltage Direct Current Circuit from the Canadian Border to New York City*, Ruling Establishing Schedule and Hearing Procedures (May 8, 2012)("Ruling on Schedule"). IPPNY's reply brief uses the point headings and uniform table of contents that Your Honors, in the Ruling on Schedule, required the parties to develop for initial and reply briefs.

the Joint Proposal ("JP") filed with the Commission on February 24, 2012 by the Applicants and the record of this proceeding.[2]

In its initial brief, filed on August 22, 2012, IPPNY demonstrated that the Commission should deny Applicants' Certificate for their proposed transmission project that would run from the Canadian border directly to Astoria, Queens (the "Project") because the Applicants have failed to meet their burden under Article VII to prove "the basis of the need for the facility,"[3] that the Project "conforms to a long-range plan for expansion of the electric power grid . . . which will serve the interests of the electric system economy and reliability,"[4] and that the "facility will serve the public interest, convenience, and necessity."[5] IPPNY demonstrated that the record evidence in this proceeding establishes that:

- The Project is not needed to meet any identified resource adequacy need;
- The Project's costs so substantially exceed its benefits that it is grossly uneconomic, and thus, cannot be financed and operated without obtaining significant subsidies – either directly or indirectly;
- The proposed certificate conditions do nothing whatsoever to prevent indirect subsidization of the project despite the evidence in the record that indirect subsidization is the most likely course for this Project;

[2] Case 10-T-0139, *Application of Champlain Hudson Power Express, Inc. and CHPE Properties, Inc. for a Certificate of Environmental Compatibility and Public Need Pursuant to Article VII of the PSL for the Construction, Operation and Maintenance of a High Voltage Direct Current Circuit from the Canadian Border to New York City*, Joint Proposal (Feb. 24, 2012).

[3] N.Y. Pub. Serv. Law §126(1)(a).

[4] N.Y. Pub. Serv. Law §126(1)(d).

[5] N.Y. Pub. Serv. Law §126(1)(g).

- The proposed certificate conditions do not adequately protect New York consumers from being required to fund the exorbitant Project subsidies in some capacity; and
- The Project also will harm the competitive generation market, associated economic development and jobs in New York, and, ultimately, New York's consumers as a whole, and such harm far outweighs any purported benefit the Project may provide.

Based on the foregoing, IPPNY demonstrated that, by definition, the Project is not in the public interest as required under PSL Section 126.1(g), and thus it must not be granted an Article VII certificate.

IPPNY hereby responds to the initial briefs that were filed on August 22, 2012 by the Applicants, Department of Public Service Staff ("Staff") and the City of New York ("NYC").[6] Initially, it must be noted that, in a desperate attempt to shift Your Honors' attention from the main issues in this case -- that the Project is grossly uneconomic and cannot and will not operate on a merchant basis, and thus, Applicants have failed to meet their burden of proof under PSL Section 126 -- the Applicants devoted a significant portion of their initial brief to a character assassination campaign against IPPNY. The Applicants attempted to paint IPPNY's position in this case, which has been focused on continuing its efforts to advance the ongoing development of the competitive electricity market and safeguarding consumers from incurring the massive subsidies that the Project will require, as instead a self-serving attempt to insulate IPPNY's members from competition. It is, however, the Applicants' claims that are self-serving -- claims

[6] Staff and NYC are signatories to the JP and supported the Applicants' request that the Commission grant a Certificate for the Project. As Staff and NYC have largely made the same arguments as the Applicants in their initial post-hearing briefs, IPPNY's reply brief will refer only to the Applicants' initial brief. Moreover, IPPNY has highlighted major points of mischaracterization and error herein. IPPNY's decision not to correct each and every error contained therein, however, should not be considered to be a concession as to any of these points.

that are completely without merit. Attacking the messenger does not change the truth of the message. Indeed, as Your Honors correctly ruled in the August 31, 2012 Ruling on Motions to Strike and to Notice, IPPNY's positions expressed (or not) in prior proceedings and Applicants' baseless speculation concerning IPPNY's motives here are irrelevant to the issues in this case.[7]

As Your Honors' ruling emphasized before testimony was filed or hearings were held in this proceeding,[8] applicants were required to demonstrate through record evidence that their Project met each of the requirements of PSL Section 126 before their Project could be awarded a Certificate. In their initial post-hearing briefs, Applicants, Staff and NYC summarily assert that the Project is needed and will provide significant economic benefits and that the proposed June 4 Certificate Conditions ensure that the Project will be constructed and operated on a merchant basis.[9] As IPPNY discussed in its initial brief and will further address herein, these assertions -- devoid of record evidence to support them -- do not withstand scrutiny and must be rejected.

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[7] Case 10-T-0139, *Application of Champlain Hudson Power Express, Inc. and CHPE Properties, Inc. for a Certificate of Environmental Compatibility and Public Need Pursuant to Article VII of the PSL for the Construction, Operation and Maintenance of a High Voltage Direct Current Circuit from the Canadian Border to New York City*, Ruling on Motions to Strike and to Notice (August 31, 2012)(denying IPPNY's motion to incorporate or take notice of IPPNY's RFI letters because "the argument over IPPNY's alleged actions or inactions in this regard is not relevant to the PSL Article VII issues that are before the Commission.") It should be noted that Staff also made similar claims in its initial post-hearing brief. *See, e.g.*, Staff Initial Post-Hearing Brief at 7 (stating, "[t]he only party presenting a witness who testified in opposition to the grant of a Certificate to the Applicants was IPPNY, an organization of incumbent competitors (whose normal bent is to attempt to keep new entrants out of the electricity supply market")). Contrary to Applicants' and Staff's false assertions, IPPNY has, in fact consistently advocated for policies that protect competitive markets and consumers from subsidized, uneconomic new entry, even in instances where such advocacy may not have been in the best economic interest of an individual IPPNY member. Based upon Your Honors' ruling that IPPNY's actions are not relevant, it is IPPNY's understanding that Applicants' assertions in this regard will be accorded no credence and Applicants' fabrications have been eliminated entirely from any consideration in this proceeding. Thus, while abundant evidence exists to correct the record, IPPNY will not respond any further to Applicants' inflammatory allegations concerning IPPNY's actions.

[8] Case 10-T-0139 - *Application of Champlain Hudson Power Express, Inc. for a Certificate of Environmental Compatibility and Public Need Pursuant to Article VII of the PSL for the Construction, Operation and Maintenance of a High Voltage Direct Current Circuit from the Canadian Border to New York City*, Ruling on Motion at 9 (May 25, 2012).

[9] The Applicants originally included merchant provisions in the JP which they claimed were sufficient. Since that time, Applicants have replaced these provisions three times. The currently proposed provisions were submitted to the Commission on June 4, 2012 and are referred to herein as the June 4 Certificate Conditions. Hearing Exhibit 150. Applicants' renewed assertions as to the sufficiency of the June 4 Certificate Conditions are belied by the

In fact, notwithstanding Applicants' clear statutory obligations and Your Honors' admonitions concerning the lack of proof in the record as late as May, IPPNY's witness, Mr. Mark D. Younger, was the only witness to put forward an analysis of the economic viability of the Project itself. In his direct and rebuttal testimony, Mr. Younger demonstrated that the Project's costs were significantly higher than its projected benefit, and thus, the Project cannot proceed forward or be operated over the long term without either directly or indirectly accessing substantial amounts of subsidization in some form. As IPPNY explained in its initial brief, Applicants cannot be allowed to avail themselves of the less stringent level of scrutiny regarding whether their Project meets the need and public interest requirements in this Article VII proceeding by falsely claiming that their Project will operate on a merchant basis when the evidence is clear that the Project cannot be merchant over the long term.[10]

The Applicants, Staff and NYC have failed to offer any evidence that the June 4 Certificate Conditions will prohibit the Applicants from receiving indirect subsidies from its shippers using the Project. For example, NYC summarily asserts that Applicants have "accepted strict obligations that collectively obligate it to develop the Facility as a merchant resource."[11] Starting from that flawed premise, NYC concludes "[s]imply put, it is not clear what else CHPE could have done to confirm merchant status."[12]

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record in this proceeding which demonstrates that the June 4 Certificate Conditions do not prohibit indirect subsidization.

[10] Remarkably, in attempting to support their claim that their Project conforms with the State's long-range plans for expanding the electric grid, Applicants specifically reference "New York's already heavily-burdened consumers of electricity." *See* Applicants' Initial Post-Hearing Brief at 75. As Mr. Younger's testimony demonstrates, unless the Certificate conditions are revised to prevent indirect subsidization as well as direct subsidization, the Project will most assuredly even more heavily burden New York's consumers.

[11] Initial Brief of the City of New York at 17.

[12] *Id.*

As IPPNY demonstrated in its initial brief, the June 4 Certificate Conditions do not prohibit Applicants from indirectly receiving funding through a contract or other mechanism created by a discriminatory procurement process. A shipper could enter into a contract pursuant to a discriminatory procurement process to sell its electricity to a New York State agency or authority, such as the New York Power Authority ("NYPA"), across the Project. The shipper would then remit some portion of the above market revenues it received under the contract to the Applicants to finance the Project. The June 4 Certificate Conditions would prohibit Applicants from entering into a contract with NYPA but would not prohibit the shipper from doing so. Neither Applicants nor any other Signatory Party have proven otherwise. If Applicants truly believe that their Project is economic and does not require subsidies and they are truly committed to constructing and operating their Project on a merchant basis, they should willingly accede to additional conditions that expressly proscribe indirect subsidization of the Project. In short, if the Applicants are true to their word they will have given up nothing in doing so.

It is disingenuous for Applicants to complain about discrimination with respect to other suppliers in New York City when they themselves have agreed to accept these conditions. To the extent there is discrimination, Applicants have elected to rely upon a less stringent review standard and now, in exchange, must accept these conditions. Applicants must accept both direct and indirect proscriptions for the June 4 Certificate Conditions to achieve their purpose. Applicants have not provided any evidence that the June 4 Certificate Conditions would be any less enforceable to its shippers than they would be to themselves. Thus, either the June 4 Certificate Conditions are enforceable and effective or they are unenforceable and effective. If

the latter, NYC and Consolidated Edison Company of New York, Inc. ("Con Edison") have made it clear in their pleadings that they would no longer support the Project.[13]

As Applicants have failed to meet their burden under Article VII to prove "the basis of the need for the facility" and -- given its grossly uneconomic nature -- cannot show that the Project will "... serve the interests of the electric system economy and reliability," Your Honors should recommend that the Commission reject the JP and deny the issuance of a Certificate to the Applicant for the Project. However, if Your Honors find that the Commission could nonetheless decide to grant a Certificate to the Project, the Commission must require the Applicants to accept a certificate condition that specifies that the Project's Certificate will be rendered null and void if the Project is able to access, directly or indirectly, a subsidy in any form whatsoever.

B. BASIS OF THE NEED

Applicants asserted that the Project will reduce wholesale market prices of electricity and wholesale market prices for installed capacity by up to $3.4 billion and $6.5 billion, respectively, from 2017 to 2027.[14] Applicants further asserted that the Project would provide production cost savings of up to $6.1 billion and reduce total emissions of SO_2, NO_x, and CO_2.[15] Applicants stated that the emissions reductions and production cost savings, by themselves, support a finding that the Project is needed.[16] Citing to the finding in a New York Board on Electric Generation Siting and the Environment ("Siting Board") decision that the proposed Brookhaven Energy Center ("Brookhaven") generating project's $27 million in production cost savings

[13] *Id.*; Con Edison Initial Brief at 4-6.

[14] Applicants' Initial Brief at 6.

[15] *Id.*

[16] *Id.* at 7.

would be in the public interest, the Applicants argued that their Project also must be found to be in the public interest.[17]

The Brookhaven Order, however, is clearly distinguishable and does not support Applicants' claim that the Project is in the public interest. The Siting Board granted Brookhaven a certificate pursuant to Article X of the PSL. One of the required findings in Article X was that "the facility was selected pursuant to an approved procurement process."[18] Relying on the precedent it had set in its Athens Generating Company Order,[19] the Siting Board determined that Brookhaven had been selected pursuant to an approved procurement process because it was a merchant plant selected by the competitive process for electric generation. The Siting Board made this finding based on Brookhaven's statement "that it would not seek to recover any costs from ratepayers under the PSL, nor would it operate as a qualifying facility and seek a contract under the Public Utility Regulatory Policies Act of 1978."[20]

The Athens Generating Company Order established the precedent that the introduction of a generating facility into the competitive electricity market satisfies the required finding that the facility is needed. IPPNY fully supports this precedent because it recognizes appropriately that new, truly *merchant* (*i.e.*, unsubsidized) entry benefits competition. Importantly, unlike in the instant proceeding, no party contested Brookhaven's statement that it would operate its project on a merchant basis. If the Siting Board had determined that Brookhaven was not able to

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[17] *Id. (citing* Case 00-F-0566, *Application of Brookhaven Energy Limited Partnership for a Certificate of Environmental Compatibility and Public Need to Construct and Operate a 580 Megawatt Electric Generating Facility in the Town of Brookhaven, Suffolk County*, Opinion And Order Granting Certificate Of Environmental Compatibility And Public Need (August 14, 2002) at 73 ("Brookhaven Order")).

[18] PSL § 168(2)(a)(ii).

[19] Case 97-F-1563, *Athens Generating Company*, Order Concerning Interlocutory Appeals (January 28, 1999) at 4 ("Athens Generating Company Order").

[20] Brookhaven Order at 9.

proceed on a merchant basis, it would not have been able to find that it was selected pursuant to an approved procurement process. In this case, IPPNY has demonstrated that the Project will not be merchant and that its introduction into the competitive market will actually harm that market, not benefit it as a merchant project would. Thus, the Brookhaven Order is, in fact, inapposite to the Applicants' circumstances in this proceeding.

In fact, the Project is, to the contrary, actually analogous to a $30 million transmission line that New York State Electric and Gas Corporation ("NYSEG") had proposed under Article VII in Case 92-T-1018.[21] In the NYSEG Order, the Commission withheld certification of NYSEG's proposed transmission line because it was "deeply concerned that the benefits associated with satisfying that criterion are significantly lower than the anticipated costs of the proposed transmission line."[22]

As IPPNY demonstrated in its initial brief, Applicants have vastly overstated the Project's production cost savings.[23] Moreover, while Applicants are correct that Mr. Younger determined that the Project would provide some level of production cost savings, the relevant point is that those savings are significantly lower than the costs of the Project that consumers will ultimately be required to bear in some capacity in the future to finance the Project. Once the errors embedded in the Applicants' production cost savings analysis are corrected, it, too, reveals the same thing. This adverse impact on consumers outweighs any of the Applicants' claimed benefits, including the emissions benefits. Thus, as it did in the NYSEG Order, the Commission

[21] Case 92-T-1081, *New York State Electric and Gas Corporation - Transmission Line from Brothertown Road Substation to Richfield Springs Substation*, Opinion and Order Concerning Brothertown Road Substation, Opinion No. 97-6 (May 22, 1997) ("NYSEG Order").

[22] *Id.* at 3.

[23] IPPNY Initial Brief at 22.

should determine that the Project is not in the public interest at this time because its costs far outweigh its benefits by any measure.

1. Public Policy

a. Applicants Have Distorted the Commission's Policy of Favoring New Entry in Competitive Markets.

The Applicants assert that the Commission's grant of an Article VII certificate to Empire Gas Pipeline ("Empire") in Case 88-T-132 supports the Commission's finding that the Project is in the public interest.[24] Applicants state that the Commission rejected arguments by incumbent natural gas pipelines that certification of the Empire Gas Pipeline would be "wasteful and inefficient" and that the Commission instead ruled that the increased competition resulting from the new pipeline was sufficient, in and of itself, to support the finding of public need for that project.[25] As discussed above with respect to the Athens Generating Company Order, IPPNY fully supports the Commission's policy that enhancing competition satisfies the public need standard. However, a proposed project that will not compete on a level playing field -- as in the case here -- harms competition and does not satisfy the need finding.

Applicants fail to reveal in their initial brief that the Commission in the Empire Order agreed with the concerns raised by incumbent natural gas pipelines that Empire would not compete on a level playing field because it would have the ability to offer flexible rates that its competitors were prohibited from offering and, therefore, Empire would be able to unfairly undercut its competitors' rates. The Commission stated:

> fair competition is not enhanced by allowing a state regulated pipeline to design a rate that would undercut competitors whose

[24] Applicants' Initial Brief at 7-8 (*citing* Case 88-T-132, *Application of Empire State Pipeline for a Certificate of Environmental Compatibility and Public Need authorizing construction of a natural gas pipeline pursuant to Article VII of the Public Service Law*, Opinion and Order Granting Certificate of Environmental Compatibility and Public Need, Opinion No. 91-3 (March 1, 1991) ("Empire Order")).

[25] *Id*. at 8.

> federal regulators prohibit them, for good reason, from using that rate. Customers locked into contracts with Empire for transportation at a 100% demand rate - and who therefore have to pay Empire even if they transport no gas - might be motivated to buy more costly gas available through Empire rather than less costly gas available elsewhere, if purchasing that less costly gas would incur additional transportation costs. Allowing such a rate thus would permit Empire to shift to customers the risk that its line might be underutilized, and thus diminish its incentive to reduce costs. Moreover, those customers would be a prime source of subsidy for the discounted rates discussed in the next section.[26]

The Commission required Empire to adopt a rate that sets a floor under the commodity charge high enough to recover at least its return on equity and related taxes. The Commission stated that "[t]his 'modified fixed/variable' rate design makes the simple statement that if a company fails to contain its costs and loses throughput to competitors, it will not be positioned to earn its return. This rate design will provide a framework for fair competition."[27] Thus, the Empire Order demonstrates that the Commission previously has found that the introduction of a new competitor satisfies the public need standard only if such entry does not harm competition. In the Empire Order, the Commission demonstrated that it has the tools in hand and it will use them to condition its grant of a certificate to protect competition. It should do the same in this case by revising the June 4 Certificate Conditions to expressly proscribe indirect subsidization if the Commission were ultimately to decide that a Certificate may be granted to the Project.

b. Applicants' Allegation That IPPNY Proposes to Preclude New Merchant Entry if There is No Reliability Need is Wrong.

Applicants assert that IPPNY's opposition to the Project is "completely antithetical to the proper functioning of competitive markets."[28] Applicants' claim that IPPNY's actions are anticompetitive is premised on their distorted characterization of testimony Mr. Younger

[26] Empire Order.

[27] *Id.*

[28] Applicants' Initial Brief at 9.

provided on cross-examination as "concessions." First, Applicants asserted that Mr. Younger, at TR 598, lines 21-25, conceded that the Project would provide wholesale price reductions and production costs savings "but claimed that those impacts should be regarded as harms to competition rather than as benefits to consumers . . . ."[29] Second, Applicants asserted that Mr. Younger, at TR 541-555 and 592-595,

> conceded that his contentions regarding the lack of any need for new installed capacity and the resultant uneconomic nature of any new entry into downstate power markets were not limited to the Facility, but applied as well to any new generating facilities proposed for construction in New York City or the Lower Hudson Valley during the period from 2017 to 2027, including without limitation the new facilities proposed by several IPPNY members in response to Governor Andrew Cuomo's Energy Highway Request for Information.[30]

Both assertions are completely false.

Mr. Younger's testimony on lines 21-54 of Tr. 598 have nothing to do with wholesale price reductions and production costs savings. During this part of his cross examination, Mr. Younger testified that if the cost of transmission upgrades in Canada are not paid by the shipper or the Applicants, it would be an out-of-market subsidy. Moreover, Mr. Younger clearly testified that the production cost savings and energy price savings are, in fact, benefits to consumers but that these benefits were substantially outweighed by the costs of the Project that would ultimately be subsidized by consumers.[31]

Likewise, Applicants have taken Mr. Younger's testimony at TR 541-555 and 592-595 entirely out of context. Mr. Younger did not testify that no new project could be economic if

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[29] *Id.* at 3.

[30] *Id.* at 3-4.

[31] Staff's claims that "…while the adjustments proposed by IPPNY could reduce the estimated benefits, they certainly would not eliminate the wholesale energy market benefits proffered by Staff; benefits would still be experienced by the addition of the [Project]" (*see* Staff Initial Post-Hearing Brief at 46) also fail for the same reason.

there is no need identified by the NYISO. To the contrary, the basis underlying competitive markets is that merchant players will find technology-based or other mechanisms to produce electricity more efficiently and cost effectively. Mr. Younger testified that in a non-discriminatory procurement process, any contract issued thereunder will equate to market-based revenues. Tr. 537. A project awarded a contract under such circumstances is a merchant facility because there was full and open competition among existing and other potential new suppliers. If awarded to a new supplier, the new supplier has demonstrated that it has deployed strategies to be more efficient and cost effective.[32]

However, that is not the case here.[33] As Mr. Younger demonstrated, it is the grossly uneconomic nature of the Project that, by definition, makes its entry into the market anticompetitive. Simply stated, because the Project's costs greatly outweigh its benefits, its entry into the market is uneconomic. It is not the more efficient alternative; it, in fact, cannot sustain itself over the long term. The Applicants' attempt to shift Your Honors' focus away from this core fact by equating a lack of need with being uneconomic is disingenuous. On the very pages cited by the Applicant, Mr. Younger testified as follows:

> Q. Will you turn to page 17 of your Direct testimony. And, there, you testify that the project is not needed; is that correct?

[32] Staff also attempted to discredit Mr. Younger's testimony in this regard, stating, "[h]owever, while IPPNY's witness Mark Younger states his position that new facilities are not needed, individual members of the generation membership conglomerate that he represents have taken a contrary position and have submitted filings in response to a request for proposal to the Energy Highway RFP that would add new resources to CNY. Clearly, while IPPNY asserts that there is no need for new resources in CNY, individual members of the organization, and direct competitors to the [Project], believe that their new resources could be beneficial." *See*, Staff Initial Post-Hearing Brief at 17, citations omitted. However, assuming IPPNY's recommendation to the New York Energy Highway Taskforce is followed to conduct nondiscriminatory procurement processes and an IPPNY member is awarded a contract, it simply means that the winning IPPNY member successfully deployed strategies to be more efficient and cost effective.

[33] In its initial post-hearing Brief, the Applicants claim that "IPPNY faces a heavy burden to demonstrate that competitive markets will not produce an efficient result in this case." Applicants' Initial Post-Hearing Brief at 35. Applicants have it exactly backwards. As Your Honors correctly emphasized months ago, it is the Applicants that carry the burden of proof in this case -- a burden that they have woefully failed to meet.

A. That is correct.

Q. Is it your testimony that no project is needed under Article VII unless it is required for reliability needs and assessment purposes?

A. No. That is not my testimony. Tr. 541.

This exchange reveals that Mr. Younger did not make the "concessions" that Applicants claim. Mr. Younger then drives home the point that new entry is uneconomic when it cannot sustain itself through purely market revenues, and thus, is not needed because it will not foster the ongoing development of competitive markets in the following exchange:

Q. Do you agree that building a new generating facility in New York City will provide long-term benefits to ratepayers?

A. That would really depend on whether there are out-of-market contracts supporting the building of that resource or there are not. I would certainly agree that newer resources that get built would tend to be more efficient and have lower variable operating costs.

Q. So, this whole case really comes down to whether or not there is an out-of-market contract. And, if there isn't, then all of these benefits will arise and should be considered in evaluating the need for the project; correct?

A. If there was no direct or indirect out-of-market contract, then I would agree. Tr. 581.

Q. And your testimony is that it would then suppress prices. And, it's your contention that price suppression is inappropriate?

A. Yes. The two actually go hand-in-hand. The bringing in of the uneconomic supply at the time that it comes in, it ends up suppressing prices. I mean one causes the other, but they happen, essentially, simultaneously.

Q. But, the mechanism of bringing in supply and suppressing prices, that occurs if the entry is appropriate as well as if it's inappropriate; is that correct?

A. Well, if the behavior is appropriate, I wouldn't really refer to it as suppressing prices.

Q. But, it would lower prices?

A. It would lower prices. Tr. 582-583.

Mr. Younger then explained that an economic facility that reduces prices enhances competition.[34]

> Q. You state in that paragraph that the effect on price is the same regardless of whether supply comes from a generating facility or a merchant transmission facility delivering energy from another area; is that correct?
>
> A. Yes.
>
> Q. And, would that still be your testimony
>
> A. Yes.
>
> Q. That would be true if the facility was uneconomic; then it would improperly suppress price. Do you agree with that?
>
> A. Yes.
>
> Q. And, if the facility was economic, then it would reduce prices and that would be pro-competitive; is that correct?
>
> A. That's correct. Tr. 585-586.

Applicants have put forward to Your Honors a classic straw man argument. They claim that Mr. Younger testified that all entry in the absence of a reliability need is uneconomic and then blast that argument as being anticompetitive. Mr. Younger himself readily acknowledged that a workably competitive market requires new entry that is more efficient and cost effective due to technological or other innovations. What the market cannot sustain, and what the Applicants propose in this case, is grossly uneconomic new entry that will inevitably artificially suppress prices, may cause existing, more efficient, otherwise economic merchant suppliers to go

[34] Mr. Younger's testimony is entirely consistent with IPPNY's position in November, 2008 concerning the New York State Energy Plan that Applicants chose to cite in their initial post-hearing brief -- to wit, "[u]nlike the regulated paradigm, competition provides the price signals to promote an efficient level of investment in appropriate locations." Applicants' Initial Post-Hearing Brief at 9, citing to Hearing Exhibit 165.

out of business prematurely, and stymie new merchant entry that would have been more efficient.

Applicants further argue that the Commission should not substitute its judgment for that of competitive markets in determining the economic feasibility of the Project because to do so would require the Commission to forecast the various factors that determine the economics of the Project.[35] However, given the way that the Applicants have presented their case (driven by the facts and circumstances of the Project itself), the Commission is left with no choice. In any event, the Commission performs such forecasts routinely in determining rates for regulated utilities. Mr. Younger's production cost savings analysis was modeled on the same cost/benefit analysis that the NYISO uses to determine whether transmission projects are eligible to receive cost-based rates. Further, every new entrant in the New York City capacity market is required to undergo an economic assessment that is performed by the NYISO to determine whether the entrant's capacity will be mitigated pursuant to the NYISO's Buyer-Side Market Power Rules. As Applicants have overstated the harms of such forecasts, their argument should be rejected.

The issue facing the Commission in this case is how it can best ensure that a developer will not subsequently seek subsidies from captive consumers after it obtained a certificate based on its promise that its project would be merchant. If the Commission determines that there is a risk that the developer will not operate its project on a merchant basis and such operation will be uneconomic, the Commission has two options – deny the application or impose conditions that will ensure the project will remain merchant. This is exactly what IPPNY advocates in this case.

[35] Applicants' Initial Brief at 11.

c. Competitive Injury Is Not the Only Reason The Commission Should Deny the Certificate to Applicants.

Applicants assert that it is unnecessary for the Commission to protect the competitive market from uneconomic entry because (i) the June 4 Certificate Conditions prohibit Applicants from entering into a contract with any public utility or any authority, agency or other entity of the State of New York, and any municipal subdivision of the State of New York, and (ii) the NYISO's Buyer-Side Market Power Rules fully protect existing generators from any competitive injury that may result from uneconomic entry.[36] As IPPNY discussed in Section J.7 of its initial brief, the June 4 Certificate Conditions leave a gaping loophole for the Project to obtain the subsidized financing indirectly that it will need to be constructed and operated.

In support of their second claim, Applicants quote from Mr. Younger's affidavits supporting the NYISO's proposed Buyer-Side Market Power Rules at FERC.[37] As Mr. Younger stated in his affidavits in those proceedings, the purpose of the Buyer-Side Market Power Rules is to deter uneconomic entry and to prevent such entry from impacting capacity prices in New York City. First, contrary to Applicants' assertion, the Buyer-Side Market Power Rules do not fully protect existing generators from competitive harm because they still allow a new entrant that is mitigated to artificially suppress energy prices. While certainly a costly endeavor, an entity could elect to proceed forward even though it knows that it will not be paid capacity revenues. Second, new entrants that are mitigated are subject to an offer floor of 75% of the cost of new entry. This means that an uneconomic entrant can be up to 25% less efficient than a true merchant supplier and be allowed to earn capacity revenues in the market. Third, Applicants' argument that there is no reason for the Commission to address IPPNY's uneconomic entry

[36] Applicants' Initial Brief at 12-14.

[37] *Id*. at 14.

concerns in this Article VII proceeding because IPPNY can seek to strengthen the Buyer-Side Market Power Rules at FERC or seek legislative or regulatory action prohibiting it is completely unworkable. Applicants Article VII application is before the Commission now. It could take years to achieve a solution from the Legislature that would prevent uneconomic entry as effectively as the Commission must do here to meet its public interest obligations by simply requiring that the June 4 Certificate Conditions be applied to both indirect and direct subsidization.

Regardless of the effectiveness of the Buyer-Side Market Power Rules, however, Applicants' argument that the Buyer-Side Market Power Rules obviate the need for the Commission to protect the market from uneconomic entry is a red herring. The injury to existing generators from uneconomic entry is just a side effect of the real harm with which the Commission should be concerned. That concern, as IPPNY has addressed numerous times, is the harm to consumers that will ultimately be forced to subsidize the high costs of the Project through an out of market contract with a shipper. The Buyer-Side Market Power Rules do nothing to protect consumers from the subsidies that they will likely be required to pay for the out of market contract that would be required to get the Project built. Thus, Applicants' claims must be rejected.

In fact, the Buyer-Side Market Power Rules actually mean that consumers will pay an even higher price tag than if the Project were not subject to mitigation.[38] To the extent the Buyer-Side Market Power Rules preclude Applicants or the shippers on the Project from recovering their costs from the capacity market, they would need to recover more of their costs directly from consumers. Thus, Applicants' claims must be rejected.

[38] Cf. Applicants Initial Post-Hearing Brief at 17-19.

2. Reliability Needs

Applicants assert that Mr. Younger's reliance on the NYISO's 2010 RNA for his determination that generation levels in New York City are adequate through 2027 is flawed because market conditions have changed since the issuance of the RNA.[39] Applicants state that Ms. Julia Frayer determined that there is a short-term reliability need because owners of generation have announced intentions to mothball or retire over 2,000 MW of generating capacity.[40] Applicants also argue that Ms. Frayer performed an economic analysis that demonstrates that an additional 5,000 MW of generation would retire before 2017 and that there is no evidence Mr. Younger performed a similar economic analysis.[41]

Applicants' argument is without merit. As IPPNY demonstrated in its initial brief, Ms. Frayer erred in assuming that all of the generators that had filed notices of intention to mothball would permanently retire.[42] The simple point is that if market prices start to rise high enough to come even close to supporting the economics of the Project, the mothballed units will return to the market and the generation she assumes will retire will not do so. The Project is so grossly uneconomic that it will not be able to compete at the lower market prices that will result. Thus, Mr. Younger's use of the 2010 RNA is appropriate and Ms. Frayer's analysis should be rejected.

4. Black-Start

Applicants claim that the Project's provision of blackstart service can support a finding of need is without merit and must be rejected. There is no guarantee that the Project will in fact provide blackstart service. In their initial brief, the Applicants provide a recitation of Commission quotes emphasizing the importance of blackstart service as well as the

[39] Applicants' Initial Brief at 22-23.

[40] *Id.* at 23.

[41] *Id.*

[42] IPPNY Initial Brief at 36.

Commission's concern that current providers may stop providing the service, threatening reliability.[43] The Applicants then make the unjustified leap that these concerns should somehow support the issuance of a Certificate to the Project. Specifically, the Applicants claim that "the Facility is plainly needed to provide essential Blackstart Service in New York City."[44]

The Applicants conveniently ignore, however, that the record is entirely devoid of any evidence that the Applicants will provide blackstart service or that anything in the much-touted Certificate Condition 127 (or any other certificate condition for that matter) requires them to do so. Certificate Condition 127 merely requires the Applicants to "request that NYISO identify, the additional facilities required for the Certificate Holders to provide Black Start service, as well as the cost of those facilities."[45] This condition only requires that the costs and configuration of additional facilities – none of which have been proposed to be constructed – be identified. There is absolutely no requirement in Certificate Condition 127 that the Applicants must construct such facilities once they are identified, much less any obligation that they must use them to provide any service whatsoever. Similarly missing from the Record are any firm commitments from the Applicants that they will provide blackstart service independently of Condition 127.

Most remarkably, notwithstanding its own Commission's recently stated concerns with the future adequacy of these services, particularly in New York City, Staff merely states in its initial post-hearing brief,

> Certificate Condition 127 in Appendix C to the Joint Proposal deals with the circumstances surrounding the possibility that the Facility will be able to provide black-start capability. Staff wants

[43] Applicants' Initial Brief at 25-26.

[44] *Id.* at 27.

[45] *Id.*

> the Applicants to explore this possibility with the New York Independent System Operator (NYISO) and Con Edison.[46]

For these reasons, the Applicant's claim that the Facility is needed to provide the service is meaningless and cannot be used to support a finding of need for the Facility.

C. COST ISSUES

1. Record Evidence

In their initial brief, Applicants confirm that it will cost $346 million to interconnect the Facility to the TransÉnergie system.[47] Nevertheless, they claim that these costs should be excluded from the Project's evaluation because they represent that these interconnection facilities will be owned by TransÉnergie, and TransÉnergie is responsible for the costs under its OATT.[48] This is important, Applicants claim, because "TransÉnergie is prohibited by its OATT from assigning any of the costs of these upgrades to shippers using those facilities."[49] The Applicants ignore the fact that TransÉnergie, for all intents and purposes, is the shipper that will be using the Project. TransÉnergie is owned by HQ. According to both HQ and the Applicants, HQ will be the anchor tenant of the Project. In fact, HQ has stated that it "proposes to become the "anchor tenant" for the project by committing to up to a 40-year purchase of 75% of the transmission rights, effectively paying for the construction of the line."[50] As IPPNY established in its initial brief, HQ will then seek to recover these costs through any avenue available to it, namely an above-market contract with a New York entity.

In fact, HQ admits as much in its Energy Highway RFI submission, where it states that:

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[46] Staff Initial Brief at 9.

[47] Applicants' Initial Brief at 29.

[48] *Id.* at 29-30.

[49] *Id.* at 30.

[50] Exhibit 230, IPPNY-44, attachment, The New York Energy Highway Response to Request for Information (RFI) Submitted by: TDI-USA Holdings Corp. at 3.

> Finally, the project requires significant transmission infrastructure investment in New York, *and to a lesser extent Québec*, that would be funded by Hydro-Québec's long-term transmission reservation on the line and therefore would not affect transmission rates in New York.[51]

HQ recognizes correctly that transmission infrastructure will be required in Quebec and that such investment will be funded by HQ through its transmission service agreement with Applicants. Therefore, the contention that the $346 million cost to interconnect the Project in Canada will not be borne by the shippers on the line is a fiction. Likewise, the notion that HQ would finance these costs without seeking to recover its investment is incredulous. HQ, like any other business entity, cannot reasonably be assumed to be willing to make gifts to the tune of $346 million. Therefore, the Applicants' argument that the Commission should pretend that this cost is somehow not a part of the Project must be rejected.

The Applicants' argument that the Project's Canadian interconnection costs should be excluded from the Project's overall costs is not only factually inaccurate as described above but is also fundamentally antithetical to the theory underlying the production cost savings metric. As explained by IPPNY in its initial brief, the production cost savings metric is preferable to other ways of measuring a project's benefits because it measures sustainable society-wide benefits and ignores transfer payments between consumers and producers.[52] Simply put, production cost savings measures the change in the overall cost of producing a commodity. In order to accurately do that, all of a project's benefits must be weighed against all of the project's costs. No one is disputing the fact that the $346 million (as estimated by the Applicants themselves) are necessary for the Project to produce any benefits – the Project cannot operate without that

[51] Exhibit 197, Hydro-Québec Response to The New York Energy Highway Request for Information at 6 (emphasis added).

[52] IPPNY Initial Brief at 31.

expenditure. Therefore, that cost must be included in the overall costs of the Project, regardless of who will ultimately pay that cost.

2. The Project Is Not Economic.

In their initial brief, the Applicants urge the Commission to ignore the Project's economics when making the required Article VII determinations as a matter of policy.[53] The Applicants also claim that the "Commission has historically declined to opine whether a proposed merchant facility will or will not be economically viable and to rely instead on competition and market mechanisms to resolve the issue of a merchant project's financial viability."[54] Nothing can be farther from the truth. In fact, the Commission is required to inquire into a proposed project's viability pursuant to the PSL and has consistently met that requirement in previous siting proceedings.

PSL Section 126.1 plainly states that "the commission may not grant a certificate for the construction or operation of a major utility transmission facility . . . unless it shall find and determine . . . that such facility . . . will serve the interests of electric system economy."[55] Furthermore, Section 126.1 of the PSL affirmatively prohibits the Commission from granting a certificate for the construction of a major utility transmission facility unless it finds and determines, among other things "the basis of the need for the facility," which the Commission has stated "is determined by examining numerous factors, including system reliability benefits, economic benefits for customers and the State, and the achievement of public policy goals."[56]

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[53] Applicants' Initial Brief 7-10.

[54] *Id*. at 30-31.

[55] N.Y. Pub. Serv. Law §126(1)(a).

[56] Case 08-T-0034, *Application of Hudson Transmission Partners, LLC for a Certificate of Environmental Compatibility and Public Need for a 345 kV Submarine/Underground Electric Transmission Link Between Manhattan and New Jersey*, Order Granting Certificate of Environmental Compatibility and Public Need (September 15, 2012) at 42 ("HTP Order").

Therefore, not only should the Commission inquire into the economics of the Project, it is required to do so by the PSL. Otherwise, the Commission would not be able to make the required findings that the Project will serve the interests of electric system economy, nor that it would create economic benefits for customers and the State.

Despite the Applicants' statements to the contrary, the Commission has routinely followed its regulatory mandate by investigating the economics of proposed projects in the context of their certification proceedings. Applicants claim that, in Case 08-T-0034, the Commission "rejected IPPNY's contention that the Commission should substitute its judgment for the operation of competitive wholesale markets."[57] Applicants blatantly misrepresent the Commission's holding in that case. The Commission engaged in a lengthy in-depth investigation of the economics of Hudson Transmission Partners' ("HTP") proposed transmission line. In addition to examining the economic projections supplied by HTP's supporters, NYPA and NYC, the DPS presented its own witnesses to substantiate its finding that the project would, in fact, provide economic benefits. Ultimately, the Commission found that "all the cost/benefit analyses show that there are ample benefits for New York City customers arising from the operation of the HTP facility."[58] Contrary to Applicants' argument, the Commission did not reject IPPNY's position that costs/benefits must be examined carefully before granting a certificate to HTP. Instead, Staff performed a detailed review of the costs/benefits of HTP, despite that fact that HTP characterized itself as a merchant project. The Commission addressed the cost/benefit analysis and specifically determined that benefits over 40 years would exceed the costs of the facility.[59]

[57] Applicants' Initial Brief at 31.

[58] HTP Order at 45.

[59] *Id.*

In contrast to HTP, where IPPNY did not perform any of its own economic analysis and the analysis it relied upon for its position that the HTP project is uneconomic reviewed only the first 20 years of the facility's operation, IPPNY has performed its own study of Applicants' Project. As demonstrated in detail in IPPNY's initial brief, Mr. Younger's testimony established that the project is grossly uneconomic, even when studied as far out as over a 35 year period. Mr. Younger showed that the Project will cost more, and thus require subsidies greater, than any electricity price reductions it can create. Thus, Applicants' assertion must be rejected.

E. MINIMUM ADVERSE ENVIRONMENTAL IMPACTS

4. Alternative Methods to Fulfill Energy Requirements

In their initial brief, the Applicants claim that the Commission should reject the "no build" alternative in light of the claimed savings and other benefits provided by the Project.[60] However, as demonstrated at length by IPPNY in its initial brief, the Project is grossly uneconomic because its projected benefits are dwarfed by its costs. As such, no actual benefits will inure to consumers. Despite the Applicants' lip service to the merchant nature of the Project, IPPNY demonstrated that the Project will not be able to sustain itself through market revenues alone. Instead, consumers will be left to foot the bill for the Project through an extra market contract between a shipper and a New York entity with the dollars from that contract flowing right back to the Applicants. Therefore, the Commission must select the "no build" alternative, as the only foolproof way to protect consumers.

[60] Applicants' Initial Brief at 73.

J. PUBLIC INTEREST, CONVENIENCE AND NECESSITY

1. Wholesale Energy Price Savings/Production Cost Savings

The Applicants in their initial brief attempt to discredit Mr. Younger's testimony explaining why the production cost savings metric provides a more accurate picture of the Project's benefits than a ratepayer savings metric. In doing so, they misstate Mr. Younger's testimony. Specifically, Applicants' claim that "[o]n cross examination in this case, Mr. Younger conceded that NYISO's operation of the electric system in New York State continues to this date to guarantee that such Energy Price Savings will also be provided by the Facility."[61] In support of this statement, the Applicants site to a completely unrelated portion of Mr. Younger's testimony that was provided on cross examination.

Not only did Mr. Younger never make the concession that Applicants claim, this particular attack on Mr. Younger's testimony misses the point entirely. Mr. Younger does not dispute that the Project will create some amount of ratepayer savings in the short term (although Mr. Younger did demonstrate that flaws inherent in Applicants' assumptions grossly overstated the level of such savings). To the contrary, what Mr. Younger established was that the grossly uneconomic nature of the Project means that much of these energy price savings actually constitute anticompetitive artificial price suppression. As demonstrated by IPPNY in its initial brief, because the Project is so uneconomic, any price reductions that will be achieved by its operation will be massively overshadowed by its costs. The Applicants conveniently gloss over the fact that colossal subsidies that will be borne by New York consumers in some capacity will be required to achieve these highly lauded yet admittedly ephemeral price reductions. Such price reductions will be long gone and yet their price tag will remain.

[61] *Id.* at 83.

Moreover, to accurately estimate the Project's production cost savings, both the Applicants and IPPNY agree that the cost of energy transmitted over the Project is the single most important assumption that must be set when performing these analyses. The Applicants stated in their initial brief that "this adjustment represents over 70 percent of the difference between the estimates of the Production Cost Saving attributable to the Facility developed by Mr. Younger and Ms. Frayer."[62] Mr. Younger likewise confirmed that the difference between his modeling and Ms. Frayer's is largely attributable to this single issue. Tr. 507. As IPPNY demonstrated in its initial brief, the electricity that will be transmitted over the Project is not free.[63] It has associated opportunity costs that represent the revenues HQ could receive by selling the energy elsewhere.

In their initial brief, Applicants claimed that although opportunity costs do in fact exist, they are so low that the energy is still effectively free.[64] This fiction is belied by the Applicants' own CEO, Mr. Donald Jessome, who testified that HQ can and will find other revenue streams for their energy. Indeed, Mr. Jessome's statements in this regard amount to nothing other than a thinly veiled threat. He said that if the Commission does not approve the Project, all of the benefits of the low cost hydroelectricity will go to other customers outside New York. Mr. Jessome's grandstanding notwithstanding, the idea that HQ would give its energy away is absurd.

Similarly, Applicants' refusal to realistically value the energy's opportunity costs is further contradicted by HQ's own statements in response to the Energy Highway RFI. In that response, HQ stated that:

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[62] *Id.* at 89.

[63] IPPNY Initial Brief at 28-29.

[64] Applicants' Initial Brief at 87-88.

> In developing these resources, Hydro-Québec applies the principles of sustainable development from the planning phase all the way through to construction and operation. Hydro-Québec *does not undertake a project unless it is profitable* under market conditions, environmentally acceptable and favorably received by local communities.[65]

In its RFI response, HQ also identified another opportunity to deliver power into New York that does not rely on the Project. HQ proposed two separate projects in response to the Energy Highway RFI. The first was becoming an anchor tenant on the Project. The second, which HQ requested be evaluated individually, was to increase HQ power flows into New York:

> In addition to Hydro-Québec's proposed participation as the anchor tenant for the CHPE project, Hydro-Québec proposes to work in conjunction with the New York State transmission owners to optimize and expand the existing upstate New York – Québec transmission interconnections and relieve key New York congestion points. In addition to transmission upgrades in Québec, substantially increasing power flows from Hydro-Québec would likely also require transmission upgrades in New York to remove existing deliverability constraints. Increasing the transfer capability over existing interfaces would increase deliverability of upstate generation into downstate areas, including new in-state renewable generation. As identified in the STARS report, the benefits from this type of new transmission investment can be maximized with increased imports from Hydro-Québec.[66]

Thus, based on HQ's own submission, HQ will, in fact, explore other opportunities within New York should the Project not be certificated.

Still another potential route for HQ's energy is the Northern Pass Transmission Line. On February 11, 2011, FERC approved a bilateral, cost-based transmission service agreement between Northern Pass Transmission LLC ("Northern Pass") and HQ for service over the proposed Northern Pass Transmission Line.[67] Under the terms of that agreement, Northern Pass

[65] Exhibit 230, IPPNY-44, attachment, The New York Energy Highway Response to Request for Information (RFI) Submitted by: TDI-USA Holdings Corp. at 1 (emphasis added).

[66] Exhibit 197, Hydro-Québec Response to The New York Energy Highway Request for Information at 8.

[67] *Northern Pass Transmission LLC*, 134 FERC ¶ 61446 (Feb 11, 2011).

agreed to develop and construct a 1,200 MW HVDC line which will link the Hydro-Québec TransÉnergie system in Québec to the New England transmission system. Northern Pass agreed to sell 1,200 MW of firm transmission service over the Northern Pass Transmission Line to HQ Hydro over a 40-year term.

In light of HQs own statements, the documented availability of alternate export capability for HQ power, and simple common sense, the Applicants' insistence that HQ would nonetheless give away its energy if it could not deliver it over the Project is outright ludicrous. In fact, the Applicants' contention is further contradicted by their own argument just a few pages away. There, the Applicants claim that Mr. Younger's contention that the Facility will fail the NYISO's Part B test for mitigation purposes "is based on the same flawed analysis of the opportunity costs associated with the electricity delivered by the Facility."[68] What the Applicants fail to mention, however, is that the NYISO assigns opportunity costs to transmission projects when calculating a unit's Net CONE for the mitigation exemption test. The NYISO determines Net CONE for transmission projects by calculating the costs of the project based on estimates of price differences at the border – precisely what Mr. Younger did, and the Applicants attacked. These opportunity costs cannot be ignored. When they are accounted for, the Project's benefits are not significant in comparison to its substantial costs.

O. CONCLUSION

For all of the above reasons, the Applicants have failed to meet their burden under Article VII to prove "the basis of the need for the facility," that the Project will "serve the interests of the electric system economy and reliability" and that the Project is in the public interest. Your Honors should, thus, recommend to the Commission that it should reject the JP and deny the

[68] Applicants' Initial Brief at 94.

issuance of a Certificate to the Applicants for the Project. However, if Your Honors were to find that the Commission could nonetheless determine that a Certificate may be granted to the Project, Your Honors correctly recognized that the question involving the economics of the Project had a significant bearing on the ability of the Project to be a merchant facility and required a close examination in this proceeding. Given the grossly uneconomic nature of the Project as repeatedly demonstrated throughout the record in this proceeding, Your Honors should recommend that the Commission should require the Applicants to accept an additional Certificate Condition that expressly states the Certificate for the Project will be rendered null and void if the Project is able to access, directly or indirectly, a subsidy in any form whatsoever.

Respectfully submitted,

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