Comments on Agent's Report Supporting Selection

New Jersey Board of Public Utilities
Long-Term Capacity Agreement Pilot Program

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I. Introduction

West Deptford Energy, LLC ("WDE") appreciates the commitment of the Staff of the New Jersey Board of Public Utilities ("Board") and Levitan & Associates, Inc. ("Agent") to implement the Long-Term Capacity Agreement Pilot Program ("LCAPP"). The Agent and Board Staff have worked expeditiously and put substantial effort into implementing the LCAPP on the schedule provided. WDE hereby submits its comments on the LCAPP Agent's Report dated March 21, 2011 ("Agent Report") for consideration.

WDE provides a detailed analysis of the Agent Report within these comments with a specific focus on the West Deptford Energy Station ("WDES"). Based on this analysis, WDE concludes the following:

- The WDES is the prequalified eligible generator most certain to be completed given it has obtained all of the necessary real estate rights and major permits and approvals to begin construction.

- The WDES is the only prequalified eligible generator capable of and proposing to meet a 2014 in-service date, which is to be provided a weighting preference in the evaluation process.

- WDE provided the lowest cost bid of all of the prequalified eligible generators. The selection of the WDES in combination with "SOCA 1" and "SOCA 2" will save ratepayers over $400 million throughout the contract term as compared to the recommended portfolio in the Agent Report.

- The Agent failed to evaluate WDE's proposal contrary to the specific requirements of the LCAPP Law, which mandates that prequalified eligible generators be evaluated. Contract changes requested by WDE pose no risk to ratepayers as WDE would essentially pay the ratepayers each and every year of the term of the contract.

- Based on available information, the recommended projects may not be positioned to demonstrate a reasonable certainty of completion by their proposed in-service date which is required by the LCAPP Law for projects to be prequalified and considered. The uncertainty that these projects can be constructed casts significant doubt on the success of the LCAPP itself.

- The premise for selection of the third recommended project is flawed to an extent that it is questionable if the project would provide any net benefit to ratepayers.

The recommendations made in the Agent Report are done without consideration of the WDES – the most certain and lowest cost prequalified eligible generator. The WDES must be fully evaluated and a net benefit to ratepayer analysis conducted so the Board may properly consider proposals from all prequalified eligible generators in accordance with the LCAPP Law and for the benefit of the State of New Jersey and its ratepayers.

II. Executive Summary

WDE is developing the WDES, a 650 megawatt (MW) (nominal installed capacity) natural gas-fired, combined-cycle electric generating facility to be located in West Deptford Township, Gloucester County, New Jersey. WDE has secured ***all*** of the necessary real estate rights and obtained ***all*** of the major permits and approvals necessary to begin construction of the Facility. The WDES is the only combined cycle facility in New Jersey positioned to start construction in 2011 and achieve commercial operations prior to June 1, 2014.

WDE fully participated in the LCAPP process and was determined by the Agent to be a prequalified eligible generator. WDE submitted bids for consideration that would enable construction of the WDES to begin this year. Based on information contained within the Agent Report, WDE is the only bidder certain to provide the anticipated benefits beginning in 2014. As demonstrated herein, the bid provided by WDE represents the lowest cost bid received in the LCAPP process whereby, based on the Agent's Resource Clearing Price ("RCP") forecast, WDE would essentially pay the electric utilities each and every year of the Standard Offer Capacity Agreement ("SOCA"). Ratepayers would be expected to receive over $300 million in payments from WDE under the SOCA. WDE is willing to accept this "below market" pricing in exchange for certainty. In addition to receiving over $300 million in direct payments, New Jersey will receive significant additional benefits associated with the construction and operation of the WDES including additional economic, environmental and community benefits.

The Agent did not evaluate the bid from WDE due to changes requested by WDE to the proposed form SOCA. These changes are consistent with the LCAPP Law and industry standard agreements including the BGS-FP Supplier Master Agreement used by the EDCs in New Jersey. These changes are necessary to ensure the SOCA remains valid and enforceable, which is a predicate for the SOCA to provide value. Furthermore, given the pricing proposed by WDE, acceptance of these changes poses no risk to the ratepayers. These changes ensure ratepayers will receive over $300 million in payments from WDE over the term of the SOCA. The Agent must evaluate WDE's bids in accordance with the requirements of the LCAPP Law.

The projects recommended by the Agent for selection provide benefits one to two years later, are less certain to provide such benefits, and would do so at a higher cost to ratepayers. In fact, selection of the third recommended project as compared to the WDES would cost ratepayers over $400 million more throughout the contract term.

In addition to all of the other benefits provided, the WDES would provide New Jersey with the benefit of geographic diversification relative to the Agent's portfolio of recommended projects. All of the recommended projects are located within a radius of approximately 20-miles in northern New Jersey. This concentration of plants in such close proximity poses additional risk to completion of the projects and reduced energy market benefits to the State (energy market benefits become saturated). Selection of WDE provides geographic diversification resulting in a greater likelihood of success for the remaining selected bidders and broader environmental, economic, community and energy market benefits to the State.

The Agent Report lacks sufficient detail regarding the prequalification process. The methodology discussed by the Agent does not appropriately demonstrate the recommended projects provide a reasonable certainty of completion as required by the LCAPP Law. Based on available information, the recommended projects may not be positioned to demonstrate a reasonable certainty of completion by their proposed in-service date. As such, it is questionable whether these projects can be considered as part of the LCAPP.

The quantification of net benefits to ratepayers presented in the Agent Report are overstated for both the assumed RCP credit and energy market benefits attributed to each of the recommended projects. This is more pronounced for the second and third recommended projects as less benefits are associated with incremental generation. The premise for selection of the third recommended project is flawed to an extent that it is questionable if the project would provide any net benefit to ratepayers.

III. WDE LCAPP Bids

WDE submitted four Standard Offer Capacity Price ("SOCP") bids to the Agent for consideration as part of the LCAPP. WDE conditioned its bids on certain changes to the proposed form of SOCA to make the SOCA consistent with the LCAPP Law, correct out-of-market conditions and enable eligible generators to be able to rely on the SOCA. As indicated in the Agent Report, the bids from WDE were "eliminated for non-conformance"[1] and not otherwise considered or discussed in its analysis. These actions are directly contrary to LCAPP Law, which requires an analysis of the WDES for the Board's consideration as described further herein.

III.A LCAPP Law Requires Full Evaluation of WDE SOCP Bids

The failure to evaluate the WDES is inconsistent with the Agent's functions pursuant to the LCAPP Law. WDE is an eligible generator[2] and was deemed to be prequalified by the Agent.[3] WDE received notice from the Agent on March 3, 2001 that it was deemed to be an eligible generator under the LCAPP Law and that "[b]ased on this determination, the Agent can accept and will consider a Standard Offer Capacity Price Bid from West Deptford Energy, LLC for West Deptford Energy Station." As such, in combination with the Agent determining WDE is prequalified, the Agent is required under the LCAPP Law to analyze the net benefit to ratepayers provided by the WDE bids. This obligation is mandatory. The LCAPP Law clearly states the Agent is responsible for, among other things:

> "b. … The agent… shall, on behalf of the board, be responsible for… (3) recommending to the board the selection of winning eligible generators based on the net benefit to ratepayers of ***each prequalified eligible generator's*** offer price and term. Eligible generators that can enter commercial operation for delivery year 2015, are to be provided with a weighting preference in addition to the net benefit to ratepayer test…" (emphasis added)[4]

This requirement is reiterated in the Agent Report:

> "The primary activities undertaken by LAI acting as the Board's Agent have been fourfold… Fourth, to formulate recommendations for Board consideration that select winning bids ***among the field of eligible and prequalified bidders*** based on the evaluation criteria set forth in the LCAPP Law." (emphasis added)[5]

[1] Agent Report, Page 42.
[2] *Id.* at Table 4, Page 39.
[3] *Id.* at Table 6, Page 40.
[4] LCAPP Law, P.L. 2011, c. 9, 3.b.
[5] Agent Report at Page 1.

The Agent's failure to evaluate the net benefit to ratepayers provided by WDE fails to comply with the statutory requirements and presents significant flaws in the evaluation process. In this instance, concerns with the ***proposed form*** are being used as the sole reason to not evaluate the WDE bids. This is being done irrespective of the benefits presented by the WDE bids relative to the issues within the proposed form, which have yet to be considered by the Board. The form of the SOCA itself is not final as it has yet to be approved by the Board.

After issuance of the Initial Recommendations on March 15, 2011, WDE requested the Agent fully evaluate the bids from WDE on a comparable basis to other prequalified eligible generators. However, that request was denied.[6] The failure to evaluate WDE is further inconsistent with the LCAPP Law since such inaction now deprives the Board an opportunity to carry out its selection process in the manner prescribed. Specifically, the Board is directed to:

> "…the board approve the selected eligible generators ***from among the qualified eligible generators*** participating in the LCAPP for the award of board-approved long-term financially-settled SOCAs for a term to be determined by the board but not to exceed 15 years…" (emphasis added)[7]

The Agent must present an analysis of the WDES for the Board to consider as WDE is a qualified eligible generator.

III.B Changes Proposed by WDE Conform the SOCA to the LCAPP Law

The LCAPP Law ***requires*** that the order approving the SOCA be ***irrevocable*** and directs that the SOCA shall bind the electric public utilities. As explicitly stated in the LCAPP Law:

> "…(10) that the resulting SOCA shall bind the electric public utilities to the board approved SOCAs with selected eligible generators for the term of the SOCA;
>
> e. Notwithstanding any other provision of law, each SOCA shall become irrevocable upon the issuance of such order approving a SOCA; and
>
> f. Neither the board or any other governmental entity shall have the authority, directly or indirectly, legally or equitably, to rescind, alter, repeal, modify or amend a SOCA..."[8]

The termination and remedy provisions of the Final Proposed Form SOCA are directly counter to these requirements of the law. The concerns with these provisions are discussed in further detail in the letter submitted to the Board on March 2, 2011, included as Attachment A.

[6] Agent response to Question #76 on the LCAPP website (http://www.nj-lcapp.com/qa.html)
[7] LCAPP Law, P.L. 2011, c. 9, 3.c.(3).
[8] *Id.* at 3.c.(10), 3.e and 3.f.

As such, WDE took exception to the provisions within the Final Proposed Form SOCA that are contrary to the law itself.

III.C Changes Proposed by WDE Are Reasonable and Industry Standard

The changes identified by WDE to the proposed form of SOCA are standard and conform to similar contracts used throughout the industry. In New Jersey, the Board has recognized the importance of including these provisions in other contracts administered by the Board. For example, in the Basic Generation Service program, the BGS-FP Master Agreement and the BGS_CIEP Master Agreement include provisions similar to those suggested by WDE for the SOCA. In Connecticut, which conducted a similar process to develop new generation, the contract used also includes similar provisions as suggested by WDE.

As a recent example of the complications caused by not including such provisions, NV Energy, Inc. in Nevada filed a petition with the Public Utilities Commission of Nevada on March 11, 2011 to amend four long-term power purchase agreements. In particular, two of the power purchase agreements were amended as the project sponsors were unable to finance the projects due to being at risk for a change in law. This is on point with the exact provisions to which WDE took exception in the proposed form of SOCA. In its filing, NV Energy explains:

> "The amended and restated PPA, dated February 11, 2011, addresses the supplier's inability to obtain financing based on the original terms of the PPA as disclosed in Docket No. 10-02009. Specifically, certain changes were required to allocate the risk of changes in Nevada renewable energy law in accordance with other PPAs disclosed as part of Docket No. 10-02009. The restated PPA amends the original PPA to incorporate all recent changes in the standard PPA…and is expected to enable the supplier to obtain financing for the project."[9]

It is unclear why the Agent would deviate from industry standards reflected by existing Board contracts, similar arrangements in Connecticut, and recent experience in Nevada. This is especially concerning in the light of the comments received from essentially all of the generators that are participating in the LCAPP process.[10]

[9] NV Energy, Inc. Nevada PUC filing, Docket 11-03014, "Application of Nevada Power Company d/b/a NV Energy for approval of the first amendment to the Action Plan of the 2010-2029 Integrated Resource Plan as it relates to three new renewable energy contracts, four existing renewable energy contract amendments, and three new renewable portfolio-credit-only contracts", Volume 2 of 5, Page 41

[10] "… the Agent SOCA still requires that Generator bear a level of risk that contravenes the LCAPP Act, and will render the SOCA un-financeable" (NRG Reply Comments, February 25, 2011). "***To be crystal clear***, the current form of SOCA remains ***completely non-financeable*** from the standpoint of eligible generators and from the financial community." (CPV Shore, March 1, 2011) (emphasis added)

III.D Proposed Form SOCA is Discriminatory to 2014 Projects

WDE intends to commit hundreds of millions of dollars of equity and debt for the construction of the WDES this year to support a 2014 in-service date. This commitment is based on all of the permits, approvals and commercial agreements for the WDES. If selected as part of the LCAPP, one of these commercial agreements would be the SOCA. Unfortunately, the current form of SOCA provides no value given the termination and remedy provisions contained within – provisions that are contrary to the LCAPP Law. As realized by the Agent, "the likelihood of a new generation facility entering the wholesale market absent the SOCA was low."[11] It is unclear how a generator could be expected to proceed forward absent certainty the contract will remain valid.

This issue is pronounced for projects with a 2014 in-service date that will commit several hundred million dollars in 2011 – projects that under the LCAPP Law are to receive a weighting preference. Bidders with a June 1, 2015 or June 1, 2016 in-service have merely a $1 million deposit at risk compared to hundreds of millions of dollars for WDE. These bidders, several of which have previously commented that the current form of SOCA is not financeable,[12] have time to wait for ongoing litigation related to the SOCA to be resolved and will undoubtedly request amendments to the SOCA at a later date.[13] On the other hand, bidders that intend to meet a June 1, 2014 in-service date do not have the luxury of time to wait for the results of litigation related to the SOCA. Rather, tens of millions of dollars in security will almost immediately be put at risk this May (required for participation in the PJM Base Residual Auction) and hundreds of millions of dollars will need to be committed months later this year to commence construction. These funds cannot be committed in light of the proposed form SOCA provisions and ongoing litigation.

Instead of providing a preference for projects that meet a 2014 in-service date, the proposed form of SOCA excludes their participation.

III.E Fair Evaluation of the WDE Bids is Not Infeasible or Impossible

The Agent describes it as "infeasible, if not impossible… to fairly evaluate on an ***expedited basis*** the relative merits of competing bids" (emphasis added).[14] This is not the case for the circumstance facing the Agent relative to WDE. The evaluation of the apportionment of risk and reward altered between buyer and seller by the SOCA modifications proposed by WDE is simple. The SOCA modifications proposed by WDE merely ensures WDE receives certainty of capacity revenue over the term of the contract in exchange for investing hundreds of millions of dollars related to constructing and operating the WDES. The bid pricing proposed by WDE as

[11] Agent Report at Page 20.
[12] See footnote 5.
[13] Any amendments to the SOCA subsequent to Board approval that address points raised to date would invalidate the entire process.
[14] Agent Report at Page 27.

compared to the Agent RCP Forecast[15] would suggest that ***WDE would essentially pay the electric utilities each and every year of the SOCA***. This means the "risk" of the contract modifications suggested by WDE is that the electric public utilities, and thus the ratepayers, will be assured of receiving this revenue source. WDE is willing to accept "below market" payments for capacity in exchange for revenue certainty.

[15] Agent Report at Figure 12, Page 61.

IV. WDE's Proposal is Superior

The bids provided by WDE offer the Board the opportunity to facilitate immediate construction of a new generation facility deemed an eligible generator and prequalified by the Agent with an in-service date prior to June 1, 2014. WDE offered considerable flexibility with four pricing options of varying terms to allow the Board to choose the appropriate contract obligation for ratepayers. WDE offers the only proposal from among the eligible prequalified generators certain to achieve the desired benefits and outcomes of the LCAPP Law.

IV.A Most Certain to Provide Benefits

WDE has obtained all of the major permits and approvals necessary to start construction of the WDES. This includes permits or approvals from West Deptford Township, Gloucester County, New Jersey Department of Environmental Protection ("NJDEP"), Delaware River Basin Commission, U.S. Army Corps of Engineers, and the Federal Aviation Administration. The effort to secure all of the major permits and approvals for the WDES took over two years to complete. In contrast, it does not appear based on publicly available information that any of the recommended bidders have applied for an air permit from NJDEP, which is typically one of the long-lead permits. Additionally, the air permitting issues for the recommended bidders will be exacerbated and more complicated than experienced by WDE given their close proximity to one another.

WDE has fully negotiated and executed all local development agreements (e.g. PILOT) and agreements for water supply and discharge for the Project. In contrast, the recommended generators are still in the process of negotiation PILOT or Host Community Benefit packages.[16] It is unclear if the recommended bidders have obtained agreements for water supply.

WDE has secured all of the real estate rights necessary to construct and operate the WDES. This includes all of the easements necessary to access the electrical transmission system, the interstate natural gas pipelines, and the water supply/discharge facilities. It is unclear if the recommended bidders have obtained all of the necessary real estate rights.

WDE submitted a generator interconnection request to PJM in July 2006, which was assigned queue position Q90. Beyond direct interconnection facilities, PJM determined that no new network upgrades are required for the full 650 MW output of Q90 to be designated as a network capacity resource. WDE anticipates receipt of an Interconnection Service Agreement (ISA) from PJM in the next month. In contrast, two of the recommended bidders submitted interconnection requests in November 2010 and have received no study results to date. The remaining recommended bidder submitted an interconnection request in November 2007 and received re-tooled system impact study results in February 2011 indicating upgrades necessary that will take 5-6 years from execution of an ISA to be placed in-service.

[16] Agent Report at Page 77.

In comparison to the certainty of the WDES, the numerous outstanding development items for the recommended projects pose significant risk to ratepayers in recognizing the purported benefits of these recommended projects.

IV.B Only Proposal to Be In-Service In 2014

The recommended bidders propose June 1, 2015 or June 1, 2016 in-service dates. Given the development items already completed for the WDES, WDE is positioned and offered to be in-service prior to June 1, 2014, which is before the 2014/15 delivery year. As such, WDE is to be provided a "weighted preference in addition to the net benefit ratepayer test".[17]

IV.C Lowest Cost Proposal

The Agent did not evaluate the WDE bids. Nonetheless, based on the information presented in the Agent Report, WDE is able to calculate the Gross SOCA Cost, Total RCP Credit, Total Net SOCA Cost and Unit Net SOCA Cost on a relative basis using the information presented in the Agent Report for the other bidders. This is based on a 15-year pricing option provided by WDE to be comparable to the term of the contracts recommended by the Agent for the other bidders. As shown in Figure 1, WDE provides the proposal representing the ***lowest*** Net SOCA Cost on both a total and per unit basis. The Net SOCA Cost represents the "…estimated net payments between the EDCs and the generator…"[18] WDE provides more revenue to ratepayers than any of the recommended bidders.

[17] LCAPP Law, P.L. 2011, c. 9, 3.b.(3).
[18] Agent Report at Page 43.

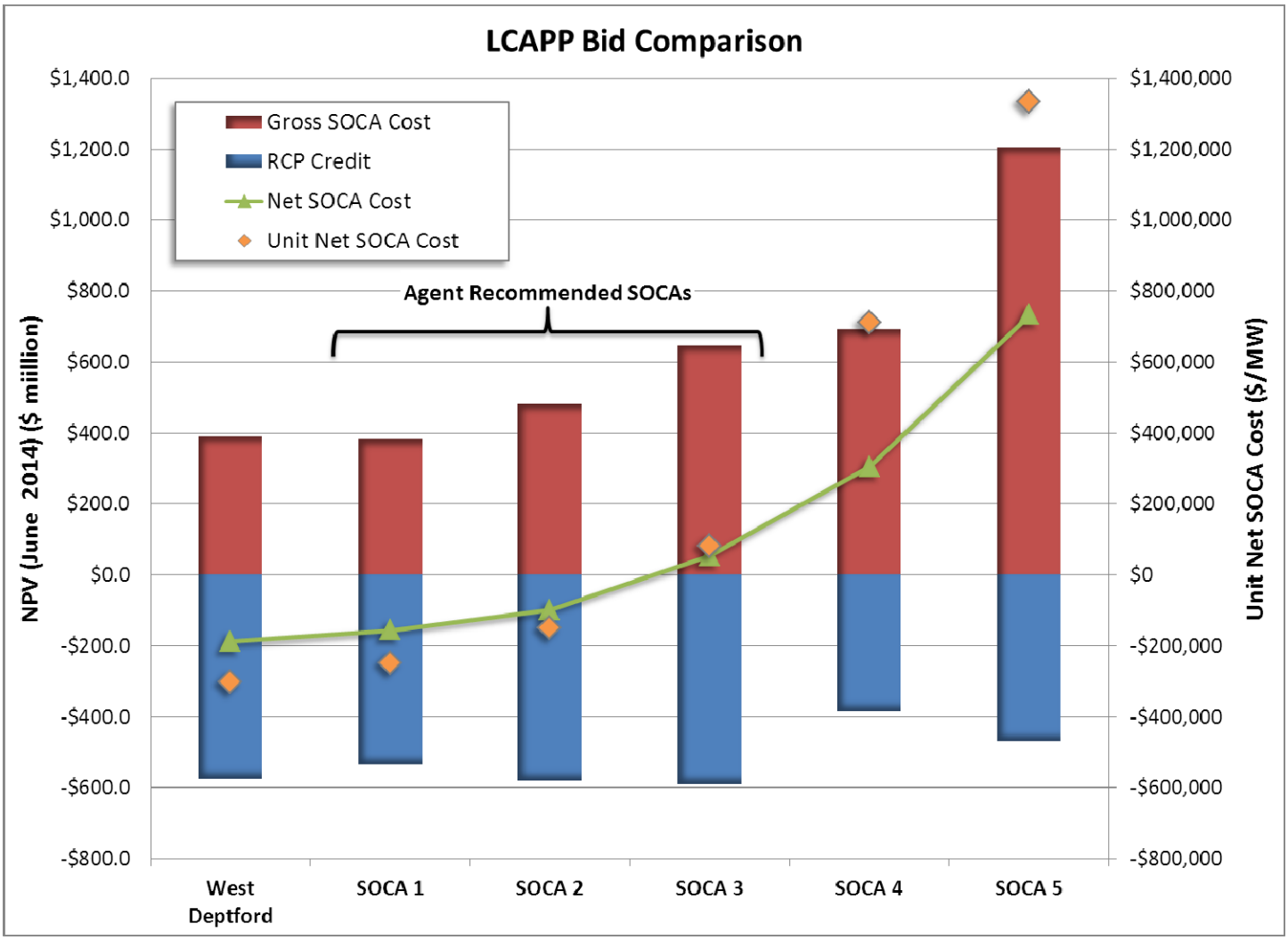

Figure 1 – LCAPP Bid Comparison

While the Total Gross SOCA Cost for WDE appears slightly higher than "SOCA 1" recommended by the Agent, this is merely due to the present value methodology used by the Agent (reference point is at the beginning of the 2014/15 delivery year).[19] The SOCA contract for WDE starts one to two years earlier than the other bidders resulting in the appearance of a higher present value cost. In actuality, the contract pricing proposed by WDE is lower than "SOCA 1" – it just begins earlier in time. The earlier start date also results in benefits accruing to ratepayers earlier in time, therefore providing higher present value benefits and overall the lowest Net SOCA Cost of all the bidders.

In order to demonstrate the cost advantage offered by WDE relative to the recommended bidders, WDE converted the cost of each bid to a nominal, levelized $/MW-day. As shown in Figure 2, the bid provided by WDE provides nearly $100/MW-day in ***revenues*** to ratepayers during the term of the contract. This represents over $300 million in payments from WDE to ratepayers over the term of the contract.

[19] Agent Report at Page 67.

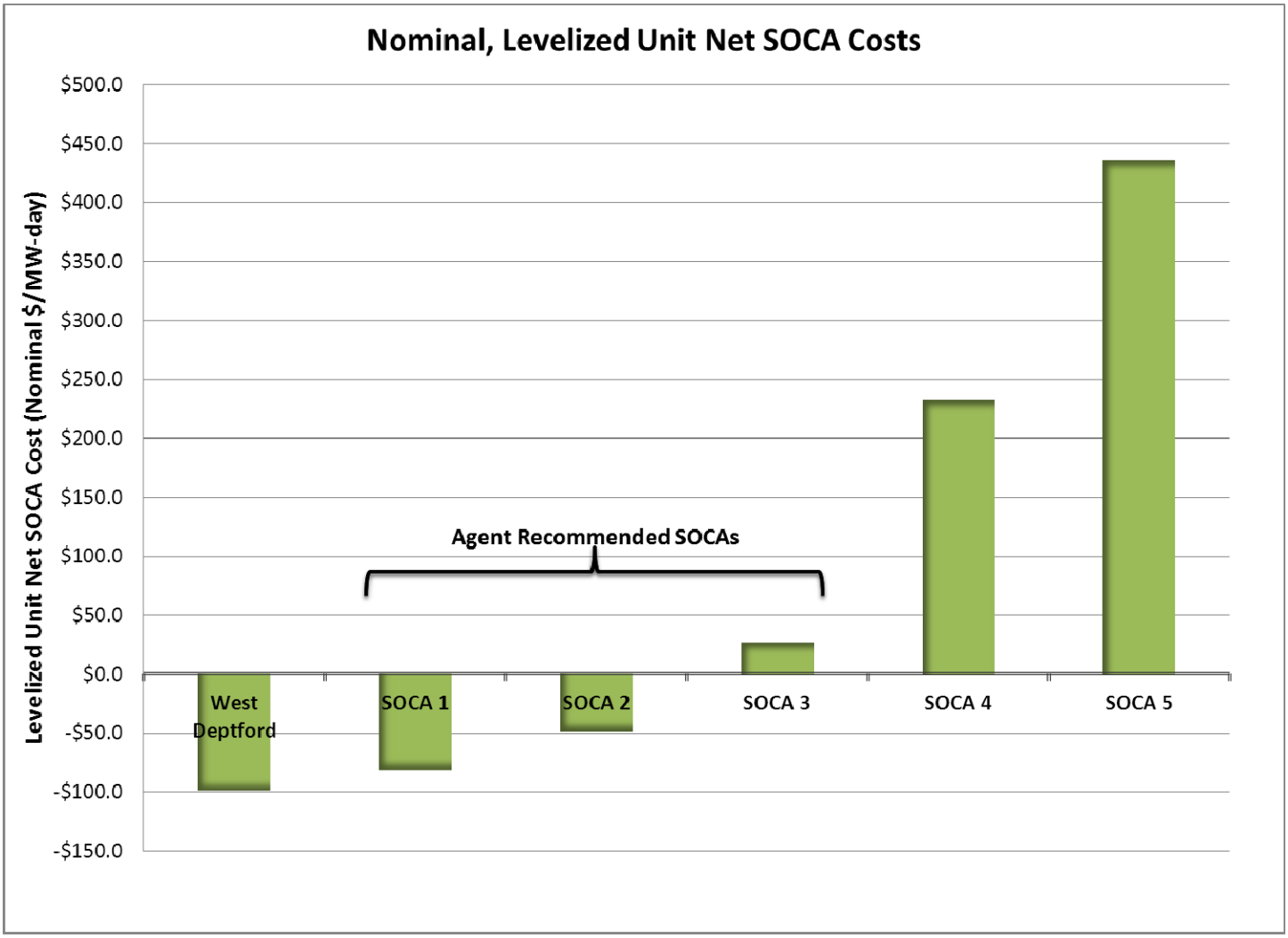

Figure 2 – Nominal, Levelized Unit Net SOCA Costs

WDE provides more revenue to ratepayers than any of the other bidders. In fact, "SOCA 3" is projected to ***cost*** ratepayers approximately $25/MW-day representing nearly $100 million in payments from ratepayers to "SOCA 3". As a result, the recommended portfolio ***will cost ratepayers over $400 million more*** during the term of the contract as opposed to a portfolio comprised of WDE, "SOCA 1" and "SOCA 2".

Based on this alone, WDE provides the most attractive proposal for New Jersey and its ratepayers without any consideration of the "pre-specified PV credit… available to eligible generators expected to achieve a COD before June 1, 2014."[20] The Agent Report does not present the value of this "credit", which would be additive to the savings identified within this Section.

[20] Agent Report at Page 66.

WDE did not conduct a comparison of energy market savings as WDE does not have access to the market simulation used by the Agent. WDE anticipates present value energy market savings for the WDES similar to, or greater than, the Agent recommended projects given the WDES will be in service one to two years in advance of the recommended projects. As such, the WDES will generate energy market savings for New Jersey ratepayers in advance of any of the recommended bidders.

IV.D Provides Geographic Diversity

In addition to providing the lowest cost proposal, WDE offers the benefit of geographic diversity relative to the portfolio of recommended bidders by the Agent. The three recommended bidders are all located in northern New Jersey within a radius of approximately 20 miles. WDE is located approximately 70 miles away in southern New Jersey and connecting to a different EDC than the Agent recommended projects. The geographic diversity offered by WDE will result in a greater likelihood of success for the remaining selected bidders and broader environmental, economic, community and energy market benefits to the State.

V. Prequalification Methodology is Flawed

The Agent Report lacks sufficient detail regarding the prequalification process. This may be due to the expedited schedule in which review and preparation of the relevant information was completed. Nonetheless, in order to evaluate whether bidders are prequalified, the Agent Report should provide detail on:

- The numerical value assigned to each color rating;
- The weighting assigned to each factor considered;
- The rating for each factor that each bidder achieved; and
- The weighted average score for each of the four LCAPP criteria for each bidder.

The lack of this detail makes it impossible to draw any meaningful conclusions regarding the efficacy of the prequalification process, if the prequalification process is consistent with the LCAPP Law, and the likelihood of achieving the desired outcome for each bidder. The Agent's prequalification process resulted in all eligible generators, which did not otherwise withdraw, being prequalified.[21] Given the development progress of the recommended projects, this fact in of itself raises concern.

V.A LCAPP Law Requires a Reasonable Certainty of Completion

The pre-qualification criterion used by the Agent does not appear to appropriately demonstrate reasonable certainty of completion for bidders. The only apparent way to fail the prequalification phase would be to receive a "Black" rating for a factor. In most cases, it appears a bidder would have to be entirely unresponsive in order to receive such a rating. The discussion of receiving a "Black" rating for each of the factors relevant to certainty of completion are presented below. As shown in Table 1, avoiding a "Black" rating by no means proves a reasonable certainty of achieving the proposed in-service date as is required by the LCAPP Law.

Table 1 - Black Rating Criteria

Factor	Agent Black Rating Criteria
Sponsor/EPC Contractor Experience	Project sponsor had no relevant experience or EPC contractor has no experience with projects utilizing proposed technology.
Financial Strength/Financing Plan	Neither sponsor nor guarantor has balance sheet strength to provide equity and no debt funding indicated
Schedule Risk	Project sponsor did not provide a schedule or if the development timelines imposed a high likelihood of not achieving the proposed in-service date
Permit Status	Timeline that is infeasible with the proposed in-service date, or provide incomplete permit

[21] Agent Report at Page 40.

	information, or will require extensive site remediation potentially incompatible with the site development schedule
Electric Interconnection Status	Interconnection Request had not yet been submitted and the project sponsor's interconnection plan was generally unresponsive
Gas Interconnection and Fuel Plan	Inadequate fuel plan that did not identify potential fuel suppliers, transportation and delivery arrangements, and did not provide an explanation of local delivery and interconnection plans
Other Risk Factors	Material projects risks that may not be mitigated, or if the sponsor has not yet achieved control of the project site

V.B Electrical Interconnection Status Review is Misguided

The most glaring concern with respect to prequalification review is related to electrical interconnection status. The discussion in the Agent Report is focused on whether a bidder could achieve the milestone to participate in the Base Residual Auction, which is merely execution of a System Impact Study (SIS) Agreement. Execution of an SIS Agreement provides no certainty as to whether the bidder will be able to achieve its proposed in-service date. As discussed in more detail below, the SIS and subsequent Facilities Study can take years to complete. Moreover, it could be years after execution of a SIS Agreement before a generator even knows what upgrades are required, which may in of themselves take several years to construct.

Based on a review of the PJM generation interconnection queue, it appears the two bidders proposing June 1, 2015 in-service dates have only recently requested interconnection with PJM and neither has received Feasibility Study results. Experience demonstrates that it takes years to progress through the interconnection queue for large-scale projects. Recent examples include WDE's interconnection request, which will take approximately 5 years from submittal of the interconnection request to execution of an ISA, and Hess's interconnection request (one of the recommended projects), which has been in the queue for nearly 4 years and just received re-tooled SIS results in February 2011. The Facility Study, which generally takes at least six months, must still be completed for Hess to reach a point where it will be in a position to execute an ISA.

The work necessary to complete the transmission facility upgrades identified throughout the PJM interconnection process will not begin until after an ISA is executed. WDE is well positioned with only direct connection facilities required to be constructed (i.e. no new network upgrades are necessary), of which construction is estimated to take 18 months. On the other hand, Hess's SIS demonstrates how long certain facilities may take to construct with some network upgrades expected to take 5-6 years from execution of the ISA.[22] These upgrades would

[22] PJM Generator Interconnection Request #T107, Impact Study (Re-tool), February 2011

be scheduled and performed by the transmission owners. Often times, it can be difficult to construct certain upgrades as outages must be carefully scheduled to maintain system reliability. The interconnecting generator is at the mercy of the transmission owner and PJM in the time it may take to construct a particular upgrade.

Based on the status of the interconnection process for the recommended projects, it is difficult to understand how a demonstration of reasonable certainty of completion by the proposed in-service date can be made as required by the LCAPP Law for any of the recommended bidders. Hess would have to execute an ISA before June 1, 2011 (unlikely based on current status in the queue) and the long-lead upgrades would have to take no more than 5 years (the lower end of the estimate in their SIS). More unexplainable is how the other two recommended bidders could reasonably be expected to achieve a June 1, 2015 in-service date given their interconnection status. It will take nearly seven years for WDE, which has no network upgrades, to progress from entering the queue to having the required interconnection facilities in-service. It will take Hess closer to ten years. Based on past experience, it is unreasonable to expect merely four years from entering the interconnection queue to having the required interconnection facilities in service for the remaining two recommended bidders especially considering there is no indication to date of the level of upgrades necessary for either of the projects. Additionally, the concentration of generation in one limited geographic area makes it more likely substantial upgrades will be required.

On the basis of interconnection status alone, the recommended projects clearly fail the "reasonable certainty of completion… to meet the desired in-service date…" as required by the LCAPP Law and therefore should not be prequalified and, as such, not considered as part of the LCAPP process.

V.C Permit Status Review Appears Limited

According to the Agent Report, a bidder is able to achieve a "Yellow" rating (second highest) for a proposed June 1, 2015 in-service date merely by indicating that major permit applications will be filed by 2Q2011. A bidder can even achieve a "Red" rating (still acceptable) where a more accelerated turnaround is assumed by NJDEP or there is ongoing site remediation that may interfere with site development.[23] It is unclear how either of these situations demonstrates a reasonable certainty of completion. For example, if a more accelerated turnaround than normal is required from NJDEP to meet the desired in-service date, how, by definition, can a determination be made that the projects have a reasonable certainty of completion by the proposed in-service date. In both cases, it is unlikely key hurdles and flaws with project development are known at this time as permit applications and supporting detail (e.g. site investigations, air modeling, etc.) have yet to be prepared. Additionally, WDE's experience indicates it will take over two years from beginning preparation of permit applications to receipt of all major permits. This would leave less than two years to complete construction which, based on discussions with engineering, procurement and construction contractors, is not feasible for a combined cycle facility.

[23] Agent Report at Page 34.

V.D Cumulative Impacts Are Not Considered

Of additional concern is the cumulative impact of the three recommended bidders progressing through the electrical interconnection and permitting processes at the same time, especially given their close proximity to one another. These projects will vie for the same set of limited resources (e.g. gas and electrical infrastructure, air quality and available offsets, permitting agency review resources) on what would appear to be an already unachievable schedule. This presents further concern regarding the reasonable certainty that these projects could be completed to meet the proposed in-service dates.

VI. Quantification of Benefits is Overstated

The Agent Report overstates the benefits provided by the recommended bidders in relation to both the RCP credit and the energy market benefits. This overstatement could lead to a recommendation of a project that may not provide net benefits to ratepayers.

VI.A Resource Clearing Price (RCP) Credit

The Agent Report presents a baseline RCP forecast[24] from which the RCP Credit is calculated.[25] The RCP forecast is not modified based on the inclusion of a bidder or, even more concerning, the cumulative impact of all of the recommended bidders. The inclusion of new generation should result in a reduction to the RCP forecast. The forecasted RCP Credit will be reduced, and more so for the second and third recommended bidders. As such, the RCP Credit is overstated. The Agent must consider the individual and cumulative impact of the recommended projects on the RCP Credit providing a more reflective indication of the anticipated net benefits to ratepayers.

VI.B Energy Market Benefits

The Agent Report presents an estimated Energy Market Price Benefit based on use of a MarketSym simulation model with EMAAC modeled as a single zone.[26] The use of what appears to be a zonal model is inconsistent with the actual nodal market operation in PJM. Furthermore, the modeling of EMAAC as a single zone (as opposed to the individual zones within EMAAC) is more concerning. The justification form the Agent Report is "… modeling EMAAC as a single zone will significantly facilitate quantification of energy price effects over the study horizon by eliminating the need to estimate transfer limit dynamics among the individual EMMAC zones."[27]

While this is a simplified approach, it overstates the energy market benefits. The zonal model assumes a system without transmission constraints within the zone – essentially a perfect dispatch model within EMAAC. This is contrary to reality in which EMAAC is one of the most constrained zones within PJM. This overstatement is more pronounced when there is a clustering of generation in a limited geographic area. This is exactly the scenario presented by the Agent Report whereby three bidders located within a radius of approximately 20-miles are recommended for approval.

WDE used the Day-Ahead Locational Market Clearing Prices Analyzer (DAYZER) cost production software and a model of the PJM system consistent with the one used by PJM to evaluate the impact of incremental generation related to energy market benefits provided. WDE evaluated the energy market benefits provided to New Jersey incrementally with and without the recommended bidders. The analysis indicates the energy market benefits from the addition of

[24] Agent Report at Figure 12, Page 61.
[25] *Id.* at Page 43.
[26] *Id.* at Page 57.
[27] *Id.* at Pages 57-58.

the first recommended bidder are substantially greater than the incremental energy market benefits for the second, and then third, recommended bidders. Figure 3 presents indicative information on the relative difference in contribution of energy savings from the recommended bidders.

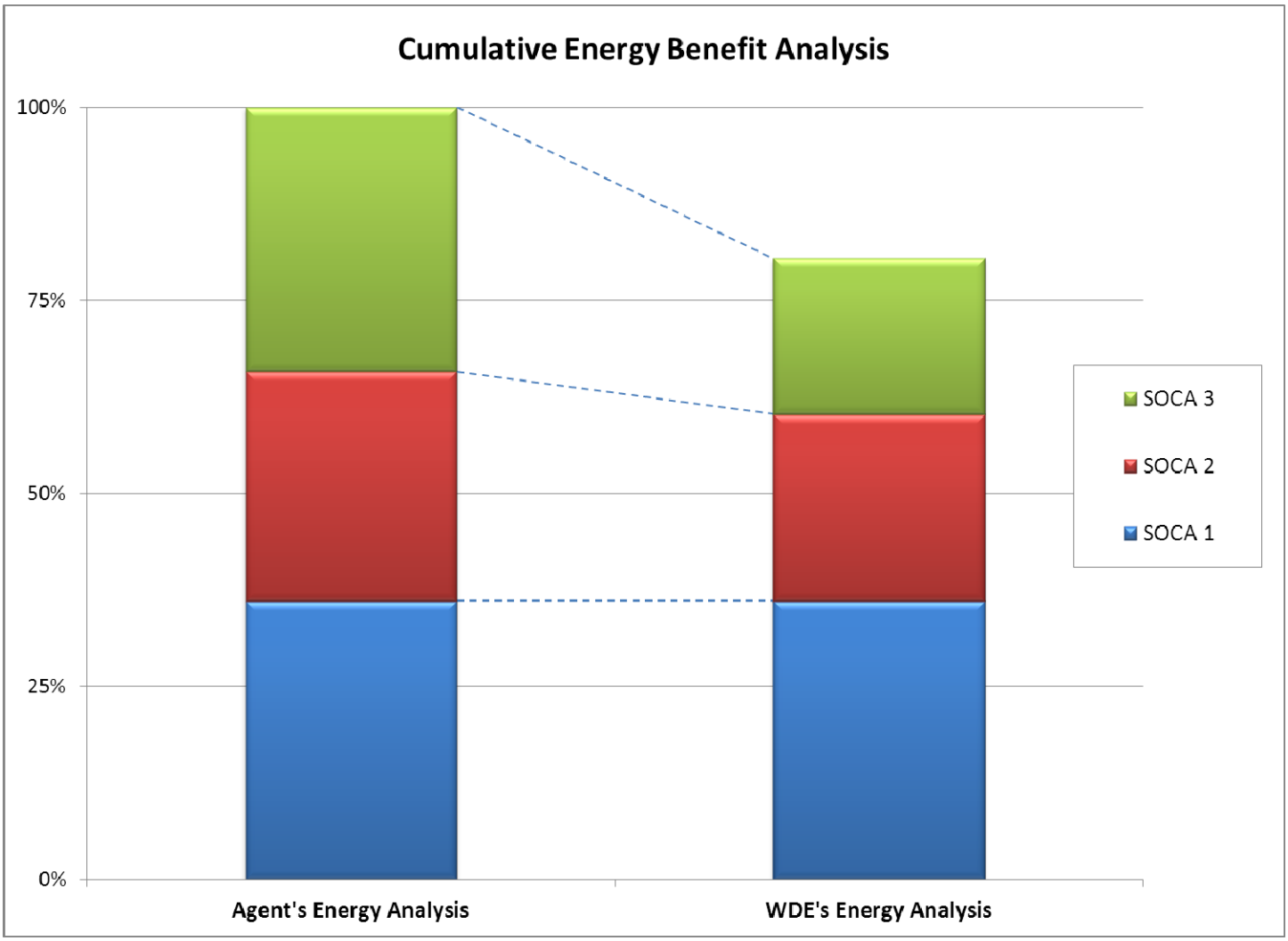

Figure 3 – Cumulative Energy Benefits Analysis

As shown, the incremental benefits of the second and third recommended bidders are approximately 40% and 55% lower, respectively, than the first recommended bidder. This is expected as the local market becomes saturated with more generation providing less incremental benefits. In contrast, the Agent's zonal model does not suggest a meaningful saturation of energy market benefits. It is understandable how a zonal model may predict such a result considering the relative size of the EMAAC zone, which consists of over 30,000 MW of generation and load. Nonetheless, the PJM market is not a zonal market and the analysis conducted by WDE indicates a substantial difference in anticipated benefits when using a simulation consistent with actual market operations. In order to reach a realistic analysis of energy market benefits to be realized by New Jersey ratepayers, the Agent must revise its

analysis to be reflective of actual expected market conditions and a more accurate net benefit to ratepayers is presented.

VII. Recommendation of "SOCA 3" is Flawed

The premise for the Agent's conclusion that the "three-generator portfolio recommended by the Agent is advantageous relative to the two-generator portfolio"[28] is flawed. As the Agent Report recognizes, the third generator has "a slightly positive Net SOCA Cost."[29] This means the Agent estimates the ratepayers will pay more for the capacity than the market revenues will otherwise generate. The "slightly positive" cost will be even more pronounced when considering the impact of the recommended bidders on RCP prices as discussed in Section V.A.

The Agent Report identifies that "Notably, Figure 13 underscores the important point that the energy market effects are roughly additive when the second and third eligible generators are combined in the recommended portfolio."[30] As discussed in Section V.B, this conclusion is based on the flawed energy market analysis that significantly overstates the energy market benefits of additive projects in a relatively small geographic area. Overall, it is questionable if the recommended "SOCA 3" will provide any net benefit to ratepayers.

[28] Agent Report at Page 70.
[29] *Id.* at Page 68.
[30] *Id.* at Page 69.

VIII. Conclusion

WDE provides, at the lowest risk and greatest benefit to ratepayers, the only proposal to bring generation to New Jersey prior to June 1, 2014. The benefits of new generation will be received one to two years earlier relative to the other prequalified eligible generators. WDE submitted the lowest cost bid in the LCAPP process whereby WDE would essentially pay the ratepayers each and every year of the SOCA. Ratepayers would stand to receive over $300 million in direct payments from WDE under the SOCA. In addition, New Jersey will receive significant other benefits associated with new generation being constructed including additional economic, environmental and community benefits from the WDES.

The Agent did not evaluate the bid from WDE due to changes requested by WDE to the proposed form SOCA. These changes are consistent with the LCAPP Law and industry standard agreements and necessary to ensure the SOCA remains valid and enforceable. These changes pose no risk to ratepayers and instead ensure ratepayers will receive the over $300 million in direct payments from WDE over the term of the SOCA.

The selection of the WDES in combination with "SOCA 1" and "SOCA 2" will save ratepayers over $400 million throughout the contract term as compared to the recommended portfolio in the Agent Report. Additionally, the WDES would provide New Jersey will the benefit of geographic diversification relative to the currently recommended bidders resulting in a greater likelihood of success for the remaining selected bidders and broader environmental, economic, community and energy market benefits to the State.

Based on available information, the recommended projects may not be positioned to demonstrate a reasonable certainty of completion by their proposed in-service date. It is questionable whether these projects can be considered as part of the LCAPP. Furthermore, the premise for selection of the third recommended project is flawed to an extent that it is questionable if the project would provide any net benefit to ratepayers.

The recommendations made in the Agent Report are done without consideration of the WDES – the most certain and lowest cost prequalified eligible generator. The WDES must be fully evaluated and a net benefit to ratepayer analysis conducted so the Board may properly consider proposals from all prequalified eligible generators in accordance with the LCAPP Law and for the benefit of the State of New Jersey and its ratepayers.

Attachment A

Letter to Board dated March 2, 2011

LS Power Group
Two Tower Center, 11th Floor
East Brunswick, NJ 08816
Tel (732) 249-6750 Fax (732) 249-7290

March 2, 2011

Via Electronic Mail

Ms. Kristi Izzo
Secretary of the Board
Board of Public Utilities
Two Gateway Center, 801
Newark, New Jersey 07102

Re: Final Proposed Standard Offer Capacity Agreement ("SOCA") – I/M/O the Long-Term Capacity Agreement Pilot Program ("LCAPP"), BPU Docket No. EO11010026 – **Immediate Attention Requested**

Dear Secretary Izzo:

LS Power Group ("LS Power") respectfully submits this letter regarding certain provisions in the SOCA to be used by LCAPP for consideration by the New Jersey Board of Public Utilities ("Board"). LS Power appreciates the opportunity to continue participating in this process and acknowledges that the Board has incorporated several of LS Power's proposed revisions into the SOCA.

Given the restrictive timeframe for meaningful review of comments on the SOCA and the LCAPP bidding deadline on Monday, ***we request immediate attention to this letter and its contents, in order to correct flaws that are "out of market", extremely problematic, and may, in fact, be insurmountable. This letter regarding the serious flaws in the SOCA draft is being sent now to allow sufficient time to be incorporated prior to bidding***.[1]

After careful review of the SOCA, and in light of Levitan & Associates' ("LCAPP Agent"), acting on behalf of the EDCs, decision not to incorporate our revisions (nor the revisions of other like-minded commenters) with respect to termination events and payments upon an early termination of the SOCA, LS Power maintains that the SOCA poses an unnecessary and very problematic barrier to the investment of capital in new generation capacity. As a result, the objectives of the LCAPP are in serious jeopardy of not being achieved to the detriment of New Jersey ratepayers.

[1] We submit this letter as part of the SOCA drafting process as well as the public comment process set out in the Board's February 10, 2011 order in this proceeding.

There are two over-all issues with the current form of the SOCA:

- **Termination Payment & Remedies**: The SOCA creates an untenable and out-of-market remedy regime where the EDCs are not held accountable for a failure to perform. For example, if the Utility does not pay the Generator under the SOCA as currently proposed, the Generator must declare an event of default, terminate the contract and pursue damages under the contract – damages limited to merely the unpaid amounts. ***The Utility—as the defaulting party for non-payment -- would pay nothing for the Generator's lost benefit of the bargain.*** Thus, the Utility could actually benefit from its own default! This is unreasonable on its face.

The Generator, having been induced by this long-term contract to build and finance new generation in New Jersey, is left with a contract that gives no recognition of the benefit of the bargain to the Generator (and, importantly, to its project finance lenders) of the capacity revenue stream over the term of the agreement. The remedies in Section 9 upon an early termination must be appropriately and commercially rebalanced to reflect traditional project finance (and legal) principles, such that the non-defaulting party receives the benefit of its bargain through the gains, losses, and costs resulting from termination (LS Power has also proposed relevant definitions).

In support of this position, LS Power previously submitted to the Board a letter dated February 28, 2011, from Union Bank which emphasizes certain long-standing principles for long-term contracts that must be considered as part of the SOCA to ensure that lenders and investors will deem a project financeable. These principles include: (1) certainty of cash flows; (2) alignment of the parties' interests to compel performance under the contract; and (3) generator liability needs to be capped up and until the point that the project is operational. We respectfully resubmit Union Bank's letter, attached hereto as **Attachment A** ("Union Bank Letter"), for your further consideration in the hope that the foregoing principles that serve as the bedrock of asset-based financing are adequately addressed in the SOCA. Indeed, as Union Bank emphasizes in its letter:

> Alignment of Parties' Interests to Compel Performance Under the Contract - the remedies that are in place to ensure that one counterparty doesn't have an incentive to cease performance under a contract need to be meaningful. The SOCA provided that a payment default by the utility would give rise to payment only of any amounts that had accrued unpaid up until the point of calculation. In order to ensure that the utility doesn't have an incentive to cease making payments if forward market conditions change from the time that the SOCA is entered into, there needs to be a meaningful termination payment that would be owed and payable to the generator. Absent such a mechanism, lenders will not have assurance that there is a meaningful penalty to compel continued performance under the contract. Union Bank Letter at 2.

These necessary revisions also must include the right to net as between the parties and within the SOCA payments. Indeed, as set out in the Union Bank letter, liability needs to be capped up to the point that the project is operational. Therefore, the

Generator's damages should be capped for an Event of Default for failure to achieve commercial operation at the amount of Construction Period Security.[2]

- **Risk of Change in Law:** Through a variety of proposed termination events, the current SOCA seeks to introduce risks not associated with the core purpose of the LCAPP, and therefore threaten the underlying purpose of the SOCA as well as the financeability of the facilities. Specifically, each proposed termination event adds unnecessary and uncontrollable risk to the generation development process posed by a prospective change in law. If any one of these events occur, it would result in termination of the SOCA, and, as indicated above, without the payment of a meaningful benefit-of-the-bargain termination payment. As indicated in the Union Bank letter, no lender would accept such potential and long-term, uncontrollable risk attached to a significant asset. Indeed, the current termination events violate a number of the core project finance principles set out in the Union Bank letter, including certainty of cash flow, the introduction of unreasonable risk of termination, and alignment of the parties' interests to compel performance. As stated in the Union Bank letter:

> The SOCA also contained language stating that if provisions of the legislation that formed the basis for the SOCA are challenged or amended, then payments or performance under the SOCA could be suspended, or certain continued representations of the generator would no longer be true. While there may currently be uncertainty around certain circumstances associated with legislation in New Jersey, once the SOCA is signed and effective and the generator is raising several hundred million dollars to construct their facility, the project finance market cannot accept the uncertain risk that these provisions place on the generator. Union Bank Letter at page 2.

In short, if the PJM rules are followed by the generator, then there should be no event of default or termination - the generator bears the risk of payment reductions, replacement capacity obligations and deficiency payments imposed by PJM under its rules.

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[2] In an analogous proceeding in Connecticut, Docket No. 08-01-01, the Department Of Public Utility Control promulgated a contract for differences for peaking generation in 2008. The terms and conditions of that contract for differences were determined in a public process along the lines of what is being conducted by the BPU, with generators and utilities providing input on what were market standard contract terms. The final contract in that proceeding, which is attached here as **Attachment C**, had a full mark-to-market, benefit of the bargain termination payment and did not provide for a termination in the event of a change-in-law. This is but one example of a contract that addresses these issues in a manner that we have highlighted herein. This contract for differences ultimately formed the basis for a successful project financing in an amount in excess of $500 million, and construction of new generation in the state of Connecticut is currently underway.

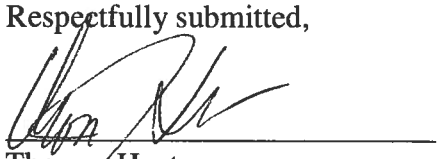
Moreover, as previously stated in our earlier comments and for the Board's consideration now, the termination provision, moreover, as proposed by the EDCs is contrary to the LCAPP Law. The LCAPP Law, P.L. 2011, C. 9, requires that the SOCA must become irrevocable upon the issuance of such order approving a SOCA. The termination provisions of the SOCA essentially take back what was given in the statute. It is our understanding that this provision mirrors provisions in Electric Discount and Energy Competition Act ("EDECA"), the 1999 New Jersey deregulation law, which were included at the urging of financing parties to ensure the recovery of stranded costs and to eliminate future risk that a law might try to undo that recovery. As required under the LCAPP Law, we need the same certainty here in the SOCA to achieve financing for the SOCA generators.

As currently drafted, in the event of a change in law, the investment required to construct the new generation facility would have already been made in reliance on the terms of the SOCA, the project could be built and operational, and yet the "one-sided" nature of the SOCA termination provisions would impose significant financial harm to the owner and lenders to the generation facility (including potential bankruptcy) while the State would continue to receive the benefits of the new, efficient, combined cycle generating capacity, including the energy savings. This creates a patently unfair dynamic.

Without fundamental revision to the SOCA's termination provisions the SOCA is extremely problematic, and may, in fact, create barriers that are insurmountable. While our opinion is based on our experience and supported by the Union Bank Letter, we encourage you to discuss with lenders on your own. Herein, LS Power outlines the provisions in the SOCA it finds problematic and states in detail its reasons for finding them so. For your convenience, LS Power has also provided a redline of the SOCA that reflects necessary changes, attached hereto as **Attachment B**.

In conclusion, LS Power respectfully requests that the Board give due consideration to the concerns expressed herein and revise the SOCA to incorporate the revisions reflected in Attachment B hereto. LS Power's proposal is supported by fundamental principles of project finance and its own experience as a participant in the project finance market. The incorporation of such revisions are critical to the success of the LCAPP and, ultimately, in the best interest of the ratepayers and the State of New Jersey. LS Power is available at your convenience to discuss any of the issues raised herein.

Respectfully submitted,



Thomas Hoatson
LS Power Group

Dated: March 2, 2011