August 4, 2010

Ms. Luly E. Massaro
Commissioner Clerk
Rhode Island Public Utilities Commission
89 Jefferson Boulevard
Warwick, RI 02888

RE: Docket 4185; Review of Town of New Shoreham Project under RI General Laws 39-26.1-7

Dear Ms. Massaro:

I am writing to you regarding Docket 4185. As a Rhode Island resident and electric power ratepayer, I would like to provide the Commission with my analysis of the expected levered internal rate of return to Deepwater Wind Block Island, LLC. In my opinion, the power prices anticipated under the Revised Power Purchase Agreement (PPA) in this docket are excessive and will provide an extraordinary return to Deepwater materially in excess of industry expectations for this nascent industry.

By way of background, I have been a principal investor and an investment banker for over 30 years. I am presently a Managing Director and head of the Special Situations Group for Morgan Keegan Equity Capital Markets. I am the founder of The Spectrum Capital Group, LLC, an investment banking firm with a national restructuring practice. Additionally, I co-founded the restructuring group at Goldman Sachs in the late 1980s and have a thorough understanding of project finance, leveraged loans, and capital structure design for publicly-traded and private companies. I hold a Bachelors degree from the University of Pennsylvania, summa cum laude. I received an M.B.A. from the Darden School of Business at the University of Virginia and a J.D. from the University of Virginia School of Law.

I have based my analysis on pre-filed testimony available to the public under Docket 4185. I have paid particular attention to the testimony of Mr. Moore, CEO of Deepwater Wind Holdings, Inc. and Deepwater's expert witnesses. I have organized this letter in a question & answer format, similar to much of the testimony you are considering under Docket 4185.

Q. Have you reviewed the proforma financials provided by Deepwater in the pre-filed testimony of William M. Moore, CEO, of Deepwater Wind Holdings, Inc.? If so, what limitations do they have?

A. Yes. I reviewed the proforma summary financial statement provided as Exhibit 1 to Mr. Moore's prefiled testimony. The proforma provide only summary income statement information and capital expenditure information. The proforma merely estimate project level cashflows without regard to the anticipated capital structures discussed by Deepwater in Docket 4111. In that docket, Deepwater indicated that it anticipated securing 80% of the construction costs for the Town of New Shoreham Project in form of commercial debt. Furthermore, Deepwater has indicated in this docket that it will apply for credit support under the US Department of Energy Loan Guaranty program. Commercial debt guaranteed by the Department of Energy will meaningfully reduce the amount of funded debt interest otherwise payable on such debt. These savings will accrue to Deepwater and not the ratepayers. Mr. Moore's financial forecast does not set forth an estimate of the cashflows available to the anticipated holders of equity and debt securities sold by Deepwater.

Q. **What is the aggregate Project Level After Tax Free Cashflow to be returned to Deepwater and its funding sources?**

A. Using Mr. Moore's financial forecast, the sum of the Project Level After Tax Free Cashflows forecasted once the project is in operation, assuming MACRS monetization, is $435,623,126. The sum of the Project Level After Tax Free Cashflows available as capital gains to Deepwater and its funding sources, net of the Facility Costs of $205,403,512, is $230,219,614.

Q. **Have you estimated the levered internal rate of return (IRR) for the project using the proforma forecast provided in Mr. Moore's pre-filed testimony and under what assumptions?**

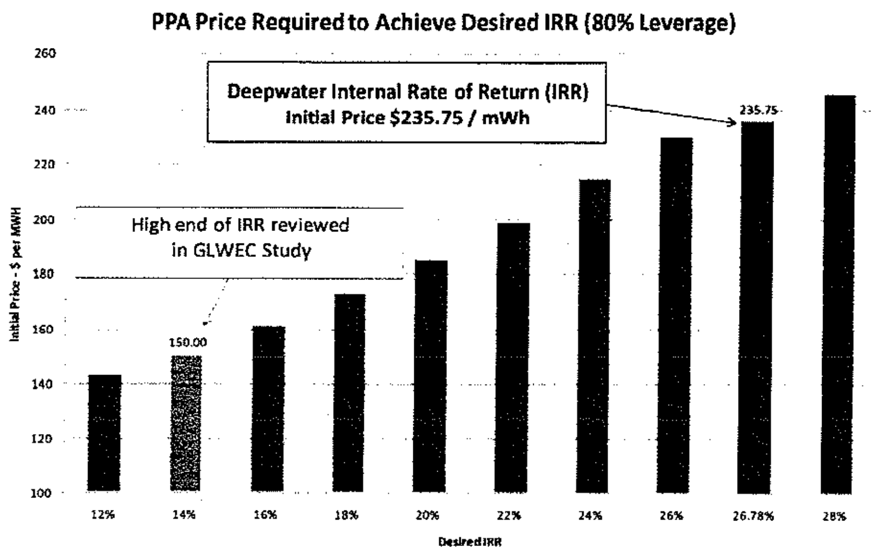
A. Yes. In order to estimate a levered IRR for the project, I have gathered market based information on capital structures, costs of capital, debt service obligations, application of the federal investment tax credit cash grants and debt guarantees by the U.S. Department of Energy Loan Program. With participation in such a loan guarantee program, I believe that Deepwater will be able to secure a debt to total capitalization for the project of 80%, with the remaining 20% derived from equity sources. Using this debt to total capital ratio and the Base Amount Facility Costs as the construction cost plus $2,000,000 in initial working capital, the amount of funded debt upon completion of the project will be approximately $165,922,810 and the amount of the equity component will be approximately $41,480,702. These figures are prior to the receipt of any investment tax credits available to Deepwater upon project completion under The American Recovery and Reinvestment Act of 2009. I have assumed cash interest expense for the debt component of the capital structure at 5.00%. I have assumed that Deepwater will receive the investment tax credit cash grant in the amount and at the time indicated in Mr. Moore's proforma forecast, $55,162,336 in November 2012. Based upon market input, I have assumed that 60% of that cash grant may be needed to reduce debt and that 40% of it will be for the benefit of the equity investors. Lastly, I have assumed an annual excess cashflow sweep to reduce debt balances of 55%, with the remaining cashflows accruing to the benefit of the equity investors. The average excess cashflow sweep equates to approximately a 1.5x debt service coverage ratio.

Q. **Using the proforma forecast provide by Mr. Moore in his pre-filed written testimony, what is your estimate of the levered IRR under your assumptions?**

A. I have estimated the levered IRR on the project under these assumptions to be 26.78%.

Q. **How does your estimate of the levered IRR change with incremental reductions in the Bundled Price of power as such term is used in the Amended PPA?**

A. Some wind farm feasibility studies have explained that it may be useful to analyze the reasonableness of initial and contract term per unit prices of power under power purchase agreements when plotted against varying IRRs (see Great Lakes Wind Energy Center Feasibility Study, April 2009, "GLWEC Study"). The chart below similarly illustrates how changes in the amount of the Block Island Wind Farm project's initial Bundled Price of power affects the project's levered IRR on the equity investment using Deepwater's proforma financial forecasts and the assumptions outlined above. Each incremental reduction in the initial Bundled Price of power under the Power Purchase Agreement reduces the projects revenue, profitability margin and corresponding Free Cashflows after tax and capital costs.



Q. **Based upon these calculations, when do you estimate that the project will return all of the equity investment to Deepwater?**

A. Based upon the capitalization outlined above, the equity investment will total approximately $41,480,702. By December 2014, the project will generate approximately $45,957,309 in free cashflow available for equity distribution. Consequently, the equity investment required to finance the project will be available to be paid back to its investors within 3 years of the project's expected completion date. All future distributions to the equity owners of the project will be returns in excess of their corpus, yet ratepayers will be paying excessively for power for another 17 years.

The power prices provided for under the Amended Power Purchase Agreement are excessive and will provide an internal rate of return well in excess of conventional and renewable energy projects under long-term guaranteed output contracts. Ratepayers will be paying excessively for renewable energy that is otherwise available. These alternatives would satisfy the State's requirement for renewal energy power sources. The Revised PPA is not commercially reasonable under Rhode Island's Long-Term Contracting Statute and should not be approved.

Sincerely,

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