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RHODE ISLAND & MASSACHUSETTS

July 1, 2010

The Rhode Island Public Utilities Commission  
c/o Ms. Luly Massaro, Clerk  
89 Jefferson Boulevard  
Warwick, RI 02888

***Re: In Re: Review Of Amended Power Purchase Agreement  
Between Narragansett Electric Company D/B/A National Grid  
And Deepwater Wind Block Island, LLC,  
Pursuant To R.I. Gen. Laws § 39-26.1-7  
Docket No. 4185***

Dear Commission:

Pursuant to the Notice Of Filing, Intervention Deadline, Preliminary Procedural Schedule, Administrative Notice, And Standards For Filings issued by the Rhode Island Public Utilities Commission ("Commission") in the above captioned Docket on June 24, 2010, please be advised that Deepwater Wind Block Island, LLC ("Deepwater Wind") will intervene as a matter of right pursuant to R.I. Gen. Laws § 39-26.1-7(b), and will be sponsoring witnesses.

**Introduction**

Deepwater Wind respectfully submits that the power purchase agreement (the "New PPA") that was filed on June 30, 2010 by The Narragansett Electric Company, d/b/a National Grid ("NGrid") is commercially reasonable and satisfies the requirements of the provisions of the Rhode Island General Laws §39-26.1-7, as amended by 2010 Senate Bill 2819 Sub A as amended, and 2010 House Bill 8083 Sub A as amended (as amended, the "New Law").

As required by the New Law, and with the exception of the following three significant changes,<sup>1</sup> the terms of the New PPA are consistent with the power purchase agreement that was filed with the Commission on December 9, 2009 in Docket 4111 (the "Prior PPA"):

- 1) The pricing provisions have been revised to reflect the provisions of the New Law. All realized cost savings are for the benefit of the ratepayer.
- 2) The Assignment clause has been revised to address the Commission's concern raised in the Order in Docket 4111.<sup>2</sup> Any assignment of the New PPA by Deepwater Wind now requires NGrid's prior consent.
- 3) During the course of the discussions respecting the New PPA, NGrid requested and Deepwater Wind agreed, to certain changes that either benefit the ratepayer or clarify NGrid's rights under the New PPA.

### **Standard of Review**

The current Docket results from the passage of the New Law. Appropriately, it directs NGrid and Deepwater Wind to obtain the Commission's approval of the New PPA. Deepwater Wind supported the New Law because it addressed two issues that arose during the litigation of Docket 4111. First, it provides clarity on the appropriate standard of review for the New PPA. The commercial reasonableness of the New PPA is to be determined by reference to "a project of similar size, technology and location, and meeting the policy goals"<sup>3</sup> in the New Law. Second, it addresses concerns raised with respect to Deepwater Wind's rate of return by mandating a transparent and open pricing mechanism. As a result, both the protections and benefits that the New PPA affords the ratepayer and the risks assumed by Deepwater Wind are unprecedented in the independent power business.

When they enacted the New Law, both the General Assembly and the Governor were aware of the New PPA pricing and the evidence submitted in Docket 4111, information that was not available to them when the Long-Term Contracting Act was originally enacted. This is noteworthy. It evidences the fact that when making the policy decision to support the Block Island Wind Farm, the Legislative and Executive branches both fully understood the potential ratepayer impacts, as well as the offsetting economic development opportunities and environmental benefits associated with the Commission's approval of the New PPA.

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<sup>1</sup> In addition to these three significant changes, certain statutory references and dates have been changed to reflect the New Law and the fact that seven months have passed since the execution of the Power Purchase Agreement filed in Docket 4111. Several typographic errors have also been corrected and the permitting schedule has been updated to reflect Deepwater Wind's current understanding of the permitting regime.

<sup>2</sup> Commission Report and Order No. 19941, April 2, 2010.

<sup>3</sup> R.I.G.L. § 39-26.1-7(c)(iv).

The New Law sets forth a standard of review<sup>4</sup> for the New PPA that differs from (i) the Commission's more typical prudency review, (ii) the standard of review for other renewable energy projects under R.I.G.L. §39-26.1-2, and (iii) the standard of review that the Commission applied in Docket 4111. The New Law directs the Commission to review the New PPA "taking into account the state's policy intention to facilitate the development of a small offshore wind project in Rhode Island waters, while at the same time interconnecting Block Island to the mainland."<sup>5</sup> If the New PPA meets the four criteria specified in the New Law,<sup>6</sup> Deepwater Wind respectfully submits that it should be approved by the Commission.<sup>7</sup>

### **The New PPA is Commercially Reasonable**

The New Law defines a "commercially reasonable" power purchase agreement for the Block Island Wind Farm as one that has the "terms and pricing that are reasonably consistent with what an experienced power market analyst would expect to see for a project of a similar size, technology and location, and [that meets] the policy goals" specified in the New Law.<sup>8</sup> This new standard clarifies the types of projects that should be referenced in determining the commercial reasonableness of the New PPA pricing by limiting those projects to small offshore wind farms.

### **Price Terms**

The New PPA pricing is materially different than the pricing in the Prior PPA. As was the case in the Prior PPA and as required by the New Law, the bundled price in the first year of the New PPA explicitly cannot exceed \$235.70.<sup>9</sup> Second, as required by the New Law, any and all realized cost savings in the development and construction of the Block Island Wind Farm result in price reductions.<sup>10</sup> Finally, the Wind Outperformance Adjustment

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<sup>4</sup> R.I.G.L. § 39-26.1-7(c).

<sup>5</sup> Id.

<sup>6</sup> Id. The four factors specified by the New Law are:

(i) The [New PPA] contains terms and conditions that are commercially reasonable; (ii) The [New PPA] contains provisions that provide for a decrease in pricing if savings can be achieved in the actual cost of the project pursuant to subsection 39-26.1-7(e); (iii) The [New PPA] is likely to provide economic development benefits, including: facilitating new and existing business expansion and the creation of new renewable energy jobs; the further development of Quonset Business Park; and, increasing the training and preparedness of the Rhode Island workforce to support renewable energy projects; and (iv) The [New PPA] is likely to provide environmental benefits, including the reduction of carbon emissions.

<sup>7</sup> As noted by the Commission in the Docket 4111 Order, the Block Island Wind Farm meets the size requirements of the New Law because the project will not exceed eight (8) wind turbines and shall have an aggregate nameplate capacity of no more than thirty (30) megawatts. R.I.G.L. § 39-26.1-7(b).

<sup>8</sup> R.I.G.L. § 39-26.1-7(d)(iv).

<sup>9</sup> R.I.G.L. § 39-26.1-7(e); New PPA, Exhibit E, Appendix X.

<sup>10</sup> Id.

Credit remains unchanged from the Prior PPA.<sup>11</sup> The resulting New PPA reflects unprecedented ratepayer benefits and protections.

#### IRR and Ratepayer Benefits

During the litigation of Docket 4111, questions were raised respecting Deepwater Wind's unlevered rate of return ("IRR"). IRR is not a factor that is to be explicitly considered in determining the commercial reasonableness of the New PPA. However, one of the significant effects of the open book pricing provisions required by the New Law is a heightened level of transparency that directly impacts Deepwater Wind's projected unlevered IRR. The New Law requires, and the New PPA provides, that to the extent that Deepwater Wind realizes cost savings during the development and construction of the Block Island Wind Farm, all of those savings benefit the ratepayer by reducing the power price paid under the New PPA. The current project cost estimates target a 10.5% unlevered rate of return for Deepwater Wind. Upon completion of the construction of the facility, Deepwater Wind's costs are independently verified to ensure that the ratepayers receive the benefit of any such savings. To the extent that there are cost savings, the New PPA price is reduced, but Deepwater Wind's return remains the same. To the extent there are cost overruns, the New PPA price is capped and is not increased, but Deepwater Wind's return will be negatively impacted. Unlike a typical open book pricing mechanism,<sup>12</sup> the risk associated with any cost overruns is borne entirely by Deepwater Wind. This one-way pricing feature, and the associated ratepayer benefit and protection, is unique to the New PPA: ratepayers benefit from cost savings and are at the same time protected from cost overruns.

This transparency and attendant ratepayer benefit continues through the term of the New PPA in the form of a Wind Outperformance Adjustment Credit. If there is more wind than anticipated by the parties to the New PPA, then one-half of that benefit is shared with ratepayers in the form of a credit that has the effect of reducing the price. However, as in the case with cost savings, this benefit is asymmetrical. Deepwater Wind has assumed all of the risk that the wind resource is less than anticipated.<sup>13</sup>

#### Competition

There was considerable discussion in Docket 4111 respecting competition. Deepwater Wind agrees that one way to determine the reasonableness of a price is through competition. However, to enable this determination, both buyer and seller need to have adequate information to both submit bids and to evaluate bids, a task that is difficult in a

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<sup>11</sup> New PPA, Exhibit E, Appendix Y.

<sup>12</sup> A typical open book pricing provision would have symmetrical provisions respecting both savings and cost overruns.

<sup>13</sup> Because of the ratepayer protections of the project cost price adjustment, although Deepwater Wind's return can increase if the wind resources enable the facility to operate at a capacity factor greater than 40%, Deepwater Wind shares half of the benefit of that increased performance with the ratepayer.

nascent industry. With large gaps in the offshore wind supply chain there remain considerable price uncertainties about several key construction and operating cost components, which leave a fixed-price bidder no choice but to include large cost contingencies in their pricing formula. Under these circumstances it makes more sense to price the first demonstration-scale project on an open-book basis, which arguably offers the ratepayer more protection by insuring that the cost of power from the facility is driven by the actual cost to build, and is not inflated by the large contingencies implicit in a fixed price bid. In addition, the State held a robust competition to select the developer judged most capable of working with the State to achieve its renewable energy goals. Seven entities participated in that competition, which resulted in the State's selection of Deepwater Wind. The New Law confirmed the reasonableness of that process by authorizing NGrid to enter into a power purchase agreement with Deepwater Wind, the State's preferred developer.

Deepwater Wind will present testimony and evidence in this Docket that the pricing in the New PPA pricing is commercially reasonable, as that term is used in the New Law. If the price in the New PPA is reasonably consistent with the price for projects of a similar size, technology and location and which meet the stated policy goals, then Deepwater Wind submits that the price should be found to be commercially reasonable as that term is defined by the New Law.

#### Non-Price Terms

In its Docket 4111 Order, the Commission found that the *terms* of the Prior PPA “with one condition ... represent what an experienced power market analyst would expect to see in transactions involving newly developed renewable energy resources.”<sup>14</sup> The sole condition about which the Commission expressed significant concern was Deepwater Wind's right to assign the agreement.

To address this concern, the New PPA has been revised to provide that Deepwater may not assign the New PPA, under any circumstances, without first obtaining NGrid's consent. In light of this change, Deepwater Wind respectfully submits that the Commission should find that the non-price terms of the New PPA are commercially reasonable.

#### **Economic Development and Environmental Benefits**

The New Law provides for the Rhode Island Economic Development Corporation and the Rhode Island Department of Environmental Management to submit advisory opinions respecting economic development and environmental benefits, both factors to be considered in approving the New PPA.

Deepwater Wind submits that the State has already benefitted from the prospect of the Block Island Wind Farm as evidenced by federal grants totaling more than \$22 million awarded to the State to support improvements to the port facilities at Quonset Point; an

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<sup>14</sup> Order at 67.

additional \$3.7 million of federal grants for workforce training in new energy related jobs; and the interest shown by some of the world's largest manufacturing companies to locate factories in Rhode Island for wind turbine assembly, submarine cable manufacture and related business activities. In addition, development of the Block Island Wind Farm, and the construction and operation of the facility, will create new direct jobs – together with the attendant multiplier effects in the local economy. Finally, the approximately 105,000 MWh of electricity produced by the Block Island Wind Farm - equal to 1.3% of the state's total annual consumption - will displace an equivalent amount of electric energy from both (a) the inefficient diesels now supplying Block Island (equal to about 10% of the wind farm's output) and (b) the least efficient, and most costly to operate, conventional generating units operating on the margin in the regional generating system (90% of the wind farm's output). This displacement effect creates both direct environmental benefits, by reducing the emission of particulates, NOx, SO<sub>2</sub>, CO and CO<sub>2</sub>, and indirect economic benefits in the form of wholesale electric price suppression effects.

**Conclusion**

During the course of this docket, Deepwater Wind will present testimony that supports its contention that the New PPA is responsive to the New Law and is commercially reasonable.

Sincerely,



Joseph A. Keough, Jr.

JAK/kf

CC: Service List (via electronic mail)