Restructuring Independent Power Contracts

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Issue Is More Than Just IPP Contracts

- Major concern is disparity between wholesale and retail electric rates
  - Retail electricity rates have, at times, approached four times the wholesale marginal electric energy costs (excluding capacity costs and ancillary service costs)
- Mistake to focus only on impact of IPP contracts on retail rates
  - Focus should be on ALL efforts to reduce retail rates
Additional Considerations

- Important considerations in addition to restructuring IPP contracts
  - securitization of stranded costs
  - retail competition
  - performance-based regulation (efficiency incentives)
  - potential closure of inefficient nuclear plants
  - potential mergers/consolidations of inefficient utilities
Historical Perspective

- QF developers entered into binding long-term contracts with utilities
- Rates based on estimates of utility’s avoided costs over 20-30 year period
- Developers entered into similarly binding contracts with fuel suppliers, steam hosts, and lenders, based upon expected stream of revenues from PPA
- Unlikely that terms of these agreements would have been the same if developers thought that power rates would be challenged subsequently
**IPP Binding Contracts**

- Fuel Suppliers and Transporters
- Utility
- Thermal Host/Site Landlord

- Transmission

- Lenders/IDAs/Equity
- Project
- Operator
Current Problems Are Unanticipated

- Avoided cost estimates appear to be wrong
  - although difficult to know where energy prices will go in future
- New pressures on utilities to reduce rates
  - particularly post-recession
- Evolution of competition in wholesale and retail markets
Hardball "Mug-a-NUG" Efforts Have Failed

- Utility tactics of using legal/regulatory means to disrupt existing contracts have largely failed
- QFs have strong legal arguments that have largely been successful
- States are preempted by PURPA from interfering with PPAs (e.g., Freehold)
- FERC has refused to seek to modify existing contracts
- No serious legislative proposal before Congress would modify existing PPAs
Practical Considerations

- New marketplace (ISO/PX) based on validity of contracts
  - Unrealistic to initiate operation of new market with abrogation of contractual commitments
  - Chilling effect on participation in market
- Alteration of PPAs has impacts beyond IPP
  - Third-party contracts
  - Steam host operations
  - Regional employment/productivity/revenues
  - Lender considerations
Successful Restructuring Through Negotiation

- Most successful attempts to alter PPA obligations have been through negotiation

  - In 1997 alone, utilities are reported to have bought out 174 IPP contracts totalling 7,442 MW (Independent Power Report, 9/5/97)

  - Master Restructuring Agreement between Niagara Mohawk and 29 IPPs

- Negotiated resolution increases pace of competition and increases savings for ratepayers
Models For Restructuring IPP Contracts

- **Niagara Mohawk model (through MRA)**
  - negotiations among utility, IPPs, and state officials
  - agreement subject to approvals of third party contractors and other conditions

- **California restructuring model**
  - negotiations among all industry participants and regulators
  - no buy-outs of IPP contracts
  - recovery through Competitive Transition Charge

- **Individual utility/IPP negotiations**
Checklist Items for Renegotiation of Power Purchase Agreements

- Third Party Approvals
  - Interconnecting and Transmitting Utilities
  - Thermal Host and Site Landlords
  - Fuel Suppliers and Transporters
  - Operator

- Financial Support Parties
  - Lenders
  - Industrial Development Agencies
  - Equity Partners
Transitional Effects of Restructuring IPP Contracts

- Consensual restructuring through negotiation is most efficient and effective
- Limited delay of ratepayer benefits during transitional period
- Hardball efforts would likely further delay savings/benefits
  - Extensive litigation
  - E.g., suspension of New Hampshire restructuring plans through temporary restraining order