LS Power

Designated Entity Agreement and Credit Support

RPPTF

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Bringing Energy Forward

Topics

- FERC Guidance
- LS Power Comments
- Historic Approach
- Letter of Credit Terms and Costs
- Alternatives

ER13-198 Background – Section 1.5.8(j)

- PJM 10/25/12 Compliance Filing:

"…Within 60 days of receiving notification of its designation… the Designated Entity shall submit … (ii) a letter of credit as determined by the Office of Interconnection to cover the incremental costs of construction resulting from reassignment of the project"

- PJM 1/29/13 Answer of PJM clarifies:

The purpose of the letter of credit is to protect ratepayers from increased costs should a Designated Entity abandon a project or default on its obligation to timely build the project due to matters within its control. In the event that a project is abandoned or there is a material default, which would justify PJM reassigning **the project** to another entity, there could be extra costs to complete **the project** or to construct an alternative project to meet the reliability need…

The letter of credit **only** would be executed upon should PJM withdraw its designation of the project as a result of a default or abandonment resulting from actions **within the control of the defaulting entity**.

To clarify, this requirement applies to *all* Designated Entities

- FERC 3/22/13 Order on Compliance

…direct PJM to submit a compliance filing to clarify that regardless whether a Designated Entity is an incumbent transmission developer or a nonincumbent transmission developer…

- PJM 7/22/13 Tariff Filing

To retain its status as a Designated Entity, within 60 days of receiving notification of its designation (or other such period as mutually agreed upon by the Office of the Interconnection and the Designated Entity), the Designated Entity (both existing Transmission Owners and Nonincumbent Developers) shall submit to the Office of the Interconnection a letter of credit as determined by the Office of Interconnection to cover the incremental costs of construction resulting from reassignment of the project, and return to the Office of the Interconnection an executed Designated Entity Agreement containing a mutually agreed upon development schedule.

LS Power 8/21/13 Filing

- Letter of Credit Vague
  - “as determined by the Office of Interconnection”
- PJM using Letter of Credit to “suppress the strategy to erroneously and excessively underbid a transmission project,” off the mark
  - Costs are only estimates and PJM preforms independent cost review
  - Incremental costs not ascertainable
- Guidance from Section 4.2.1 of TOA

Historic Approach

- Project approved by PJM board
- Under Section 4.2.1 of the CTOA, the Transmission Owner is relieved of its obligation:

Subject to: (i) the requirements of applicable law, government regulations and approvals, including, without limitation, requirements to obtain any necessary state or local siting, construction, and operating permits; (ii) the availability of required financing; (iii) the ability to acquire necessary right-of-way; (iv) the right to recover, pursuant to appropriate financing arrangements and tariffs or contracts, all reasonably incurred costs, plus a reasonable return on investment; and (v) other conditions or exceptions set forth in the Regional Transmission Expansion Planning Protocol, Parties designated as the appropriate entities to the PJM Region specified in the Regional Transmission Expansion Plan or required to expand or modify Transmission Facilities pursuant to the PJM Tariff shall construct and own or finance such facilities or enter into appropriate contracts to fulfill such obligations.

- No credit support provided to PJM

Letters of Credit Costs

- Issuance costs
- Consumes credit capacity of borrower
- Makes overall borrowing cost higher
- Risk of draw conditions
- Ultimately costs flow to ratepayers

Alternatives

- Alternative 1: Credit support (Letter of Credit, Guarantee, etc.) in amount of estimated project cost
- Alternative 2: Credit support in amount of difference between proposal and next most expensive proposal
- Alternative 3: Credit support in terms of fixed percentage of overall project cost, such as 3%
- Alterantive 4: Rights to project assets

Benefits and Disadvantages

- Alternative 1: Credit support (Letter of Credit, Guarantee, etc.) in amount of estimated project cost
  - Unreasonable amount of protection will come at too high of a cost, not financeable
  - Not consistent with "the incremental costs of construction resulting from reassignment of the project"
- Alternative 2: Credit support in amount of difference between proposal and next most expensive proposal
  - Perverse consequence of ***penalizing*** low cost projects (What if $50 million project selected and next most expensive project is $150 million?)
  - Credit support could be higher than entire cost of the proposal – not financeable
  - Unreasonable amount of protection will come at too high of cost
  - The next most expensive proposal will not necessarily move forward
- Alternative 3: Credit support in terms of fixed percentage of overall project cost, such as 3%
  - Would be financeable
  - Provides significant protection - $3 million for a $100 million project
  - Credit protection proportional to project size
  - Provides protection without unreasonable premium
- Alternative 4: Claim on project assets
  - Provides protection without unreasonable premium

Recommendation

- Entities are already qualified financially, technically
- Only need protection from default, abandonment within control
- Alternative 4: Claim on project assets
  - Protects against default
  - No unreasonable credit premium
  - Addresses all potential costs identified in PJM 1/29/13 Answer:

    …These could include the costs to: (i) purchase the right of way from the original developer; (ii) engineer into the replacement Designated Entity's plans of the partially built facilities; or (iii) purchase new easements as a result of the expiration of options that had expired. The letter of credit only would be executed upon should PJM withdraw its designation of the project as a result of a default or abandonment resulting from actions within the control of the defaulting entity.
- Alternative 3: Credit support in terms of fixed percentage of overall project cost, such as 3%
  - Will be greater than costs identified above, if any