Department of Legislative Services

Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE

Senate Bill 558 (Senator Pinsky, *et al.*)
Finance

Public Service Commission - Long-Term Power Purchasing Agreements - Renewable Energy

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This bill requires electricity suppliers of standard offer service (SOS) to enter into long-term power purchasing agreements for electricity from Tier 1 renewable resources. By October 1, 2011, each electricity supplier of SOS in the State must issue a request for proposals (RFP) for long-term power purchasing agreements; they must enter into at least one such agreement by October 1, 2012. Power purchasing agreements must be made at a definite price for a period of at least 20 years. The Public Service Commission (PSC) may waive the requirement if an electricity supplier demonstrates that such agreements are not cost-effective over a period of 25 years. In determining if an agreement is cost effective, PSC must consider specified compliance fees or penalties that the supplier would be required to pay in the absence of the agreement and the cost of operating a fossil fuel generating facility over the entire life cycle – including maintenance costs, pollution control, and decommissioning costs. PSC may not grant a waiver if the electricity supplier will receive a competitive advantage as a result of the waiver.

Fiscal Summary

State Effect: None. PSC can implement the bill with existing budgeted resources.

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Current Law: SOS is provided by local electric companies (*i.e.*, investor-owned utilities) who own the "wires" portion of the electric system. To obtain the best price for

SOS for residential and small commercial customers, PSC may require each electric company to obtain its electricity supply for SOS through a competitive process. PSC may also require or allow an investor-owned electric company to procure electricity for these customers directly from an electricity supplier through one or more bilateral contracts outside the competitive process. Under the Code of Maryland Regulations (COMAR 20.52.04.01), PSC determines the model RFP to be used for SOS electricity procurement and electric companies submit a utility bid plan based on the model RFP. The model RFP may not be altered unless it is necessary to conform to utility-specific conditions.

PSC is currently considering Case Number 9214 to investigate whether it should exercise its authority to order electric companies to enter into long-term contracts to attract new generation or to construct, acquire, or lease and operate new generation facilities in the State. In the proceeding, PSC is examining the broad policy areas surrounding SOS procurement. PSC has received comments on the scope of proposals for new generation to be submitted by interested parties and expects to set a deadline to receive proposals sometime in 2010. In the case, PSC is expected to examine location, generation technology, capacity, terms of long-term contracts, and other factors.

Maryland's Renewable Energy Portfolio Standards (RPS) requires all electricity suppliers to meet a portion of their energy supply needs with eligible forms of renewable energy by accumulating "renewable energy credits" (RECs) created from various renewable energy sources classified as Tier 1 and Tier 2 renewable sources. Examples of Tier 1 sources include solar; wind; qualifying biomass; methane from anaerobic decomposition of organic materials in a landfill or wastewater treatment plant; geothermal; ocean, including energy from waves, tides, currents, and thermal differences; a fuel cell that produces electricity from a Tier 1 renewable source; and a small hydroelectric plant of less than 30 megawatts and poultry litter-to-energy. Examples of Tier 2 sources include hydroelectric and waste-to-energy. If electricity suppliers are unable to meet RPS through purchasing RECs, they must pay an alternative compliance fee to the Maryland Strategic Energy Investment Fund within the Maryland Energy Administration.

Background: At the inception of electric restructuring, many expected acceleration in the development of competitive power plants not tied to a traditional distribution facility, so-called merchant plants. However, construction of these plants has had difficulty in obtaining sufficient private financing to proceed to construction for two reasons – the dearth of capital available in a severely strained economy, and uncertainty in the ability of a merchant plant to remain profitable over the long term needed to finance its construction. A long-term power purchasing agreement between an electric company and an individual seeking to construct an electric generating facility in the State will likely facilitate a project in obtaining financing.

Electric companies that provide SOS obtain electricity supply through a competitive process for residential and small commercial customers that participate in SOS. Electric companies are required to procure electricity for residential and small commercial customers through one or more bilateral contracts. The investor-owned electric companies submit bids to supply anticipated SOS load for residential and small commercial customers, as part of a portfolio of blended wholesale supply contracts. Current SOS contracts for residential and small commercial customers are all two years in length. SOS contracts for medium-size commercial customers are three months in length. The blended portfolio mitigates the potential for sudden retail price changes due to volatile whole market conditions. Additionally, in order to prevent an excessive amount of load from being exposed to upward market price risks and volatility, PSC may stagger the dates of the wholesale auctions.

Small Business Effect: Requiring electric companies to enter into long-term power purchasing agreements with Tier 1 renewable generating facilities may allow these projects to obtain more favorable financing and may result in additional facilities being constructed. As a result, small businesses involved with the manufacturing, distribution, and installation of solar, wind, and other renewable energy sources stand to benefit from requiring long-term power purchasing agreements.

Electric rates of small businesses that receive electric supply through SOS may be impacted as a result of the bill. As of December 31, 2009 168,335 commercial and industrial electric customers were receiving electricity supply through SOS. This represents approximately 70% of commercial and industrial customers. The exact number of commercial and industrial electric customers that are considered small businesses is not known. If the bill increases the cost of SOS electricity significantly, these businesses may switch to a competitive electric supplier instead of procuring electricity from an SOS supplier. On the other hand, if a long-term power purchasing agreement provides a significant reduction in the cost of SOS, additional businesses may switch to SOS supply.

Additional Comments: The language in the bill referring to "suppliers of SOS" may be interpreted as either being the electric companies (investor-owned utilities) that administer SOS, or the competitive electricity suppliers that are selected through a competitive bidding process to provide the electric commodity for SOS customers. This fiscal estimate assumes that the bill intends to require electric companies to procure a portion of the total SOS demand through a long-term power purchasing agreement and purchase the rest of SOS demand through the existing competitive bidding process.

Under an alternative interpretation of the bill, it may require the electricity suppliers who bid to supply the electric commodity for SOS customers to procure long-term power purchasing agreements. SOS supply is currently bid through a blended portfolio of two-year contracts for small commercial and residential customers and three-month contracts for medium size commercial customers. Requiring electricity suppliers who bid into short-term contracts for SOS supply to enter into long-term power purchasing agreements may reduce the number of electricity suppliers who bid to supply SOS.

As drafted, the distinction between "electric companies" and "suppliers of SOS" has additional implications that should be considered. The bill specifies that RPS compliance fee payments, among other things, must be considered when determining cost effectiveness of an agreement. Technically speaking, RPS compliance and power purchasing agreements are wholly separate issues. RPS compliance is met through purchasing RECs, which are commodities equal to one megawatt-hour of electricity generated from renewable sources. A long-term power purchasing agreement does not necessarily require RECs associated with that production to be sold to the same party purchasing the electricity. As a result, any electricity supplier that enters into a long-term power purchasing agreement will still be required to either purchase RECs or pay an alternative compliance fee to meet the RPS requirements.

To the extent that long-term power purchasing agreements result in the construction of additional renewable facilities, however, they could increase the supply of RECs and reduce reliance on alternative compliance fee payments for RPS compliance.

Nevertheless, the cumulative impact of the bill depends greatly on the terms of each long-term power purchasing agreement entered into by electric companies for SOS supply. Long-term supply agreements provide price stability but may be more or less costly depending on future prices of electricity. The amount of any potential price impact will depend on the amount of generation purchased through the long-term agreement, the rate negotiated in the agreement, and future market prices of electricity.

Additional Information

Prior Introductions: None.

Cross File: None.

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