

Getting Closer To A National Transmission Grid

The Editor interviews **Howard Shafferman**, Co-Chair of Ballard Spahr Andrews & Ingersoll, LLP's Energy and Project Finance Practice Group.

Editor: Please tell our readers about your background. You were Chief of Staff and Counselor of the Federal Energy Regulatory Commission (FERC) from 1990 to 1993 and have been active in various capacities in shaping U.S. energy policy.

Shafferman: I had the privilege of being at FERC at a time when the restructuring of the natural gas pipeline industry was being completed and the brave new world of electricity competition was just beginning. I was able to participate in some of the major rule-makings on the gas side and also the initial orders that provided support for a more competitive electric generation sector. The lessons learned during my tenure there have turned out to be invaluable.

Editor: Please describe the energy practice at Ballard.

Shafferman: Our group's co-leaders are in Washington. We have about 18 active members and about 15 other regular participants. Eight of our twelve offices have active members, particularly in Philadelphia, Washington, D.C., and in the West. Our firm has the distinction of having a number of offices in the West (which is rich in renewable energy resources such as solar and wind) that can provide on-the-ground support for energy project work.

Our work is both regulatory and transactional in nature. Our energy regulatory practice focuses on federal and state electricity regulation but we also do hydroelectric, oil pipeline, and natural gas work. We are probably best known for our long-time representation of ISO New England, the system operator for New England's electrical system. We also do some work for the New York independent system operator. We have especially deep experience with electric transmission and market issues.

Our transactional group focuses on project development and finance, representing project developers, utilities, underwriters, and lenders. Our active utility finance groups are in Philadelphia, Salt Lake City and Washington, D.C. Our strategic transactional focus currently is on renewables, M&A, and (more recently) carbon-risk assessments for utilities, generators, and industrial companies that own carbon-emitting facilities. In the latter case, we help them consider appropriate near-term strategies given the uncertainties about the nature of future regulation of climate change. For example, if the United States goes to a cap and trade carbon credit system, how will the purchase of credits affect project economics? What costs will state utility commissions allow them to pass through to customers? We are also advising companies about installation of renewable energy facilities and energy efficiency measures on site to benefit from tax incen-



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tives as well as from the public esteem accorded good corporate citizenship. Many municipalities can now "go green" with the help of private investment, thanks to the recent extensions of federal tax incentives in the bail-out package.

Editor: How has the downturn in the economy affected energy usage in the U.S.? How will energy fit into the new administration's priorities?

Shafferman: We are not seeing a great decrease in electrical energy usage but we are seeing some reduction in utilities' proposed capital projects. Some of the independent power deals have not closed. Because electricity demand is still growing in the U.S., the mandates being issued at the state level to use renewable energy and to reduce carbon emissions will spark increased investment in renewable energy, thus providing a green jobs and economic stimulus.

A move to greater "greenness" was a strong theme in the Obama campaign, and we expect a "green jobs" program to be part of the initial Obama stimulus package. I think that you will see some energy-related legislation very quickly in 2009, though perhaps not the full cap and trade carbon regulations because that could entail increased costs not easily borne in this fragile economy. However, the legislation may well include a federal renewable portfolio standard that will require a certain percentage of every utility's generation resources to be renewable as opposed to fossil-fueled. Many states have already put renewable portfolio standards in place; some are more aggressive than others. I think another legislative initiative that Obama might pursue is the federal siting of new electric transmission lines as opposed to state-by-state siting of those lines.

Editor: Do you think that we'll ever get the electric transmission grid that we need?

Shafferman: I think that we will get to a much stronger and wider national grid because there is really little choice – lines need to go places where they don't go today to bring renewable resources to market. Also, in a number of areas of the

country, transmission construction simply hasn't kept pace with growing demand.

Editor: In this January issue where your article will appear, we are also having an interview with the general counsel of Southern California Edison, which is taking some very innovative steps to conserve energy and produce renewable energy. Are you aware of other utilities that are equally as farsighted?

Shafferman: I can think of a couple, one being our client ISO New England, Inc., which operates sophisticated bidding markets for energy and capacity. In these markets, so-called "demand response" can bid in. In other words, an entity with the ability to stop consuming a certain amount of electricity can be compensated in largely the same fashion as an entity generating the same amount of electricity. Also, energy efficiency measures can bid in to capacity markets in New England. These measures will reduce the amount of new power plants that must be built in that region.

Editor: While we have the technology for generating massive quantities of renewable energy, there are roadblocks to using it most effectively. We were just talking about one of the roadblocks, the transmission system. Would you describe some of the others?

Shafferman: Although these technologies are much "cleaner" than fossil fuels, they can nonetheless face permitting or environmental challenges. One such impediment is the Endangered Species Act and other wildlife protection statutes. Building a wind farm on a ridge where endangered birds have their habitat and where birds can be chewed up by the turbines can be challenges. Also, a lot of the better sites for renewable development are on federal lands, and the Bureau of Land Management's permitting process is quite complex and time consuming. For example, over 80 percent of Nevada is in federal hands, so if you want to locate any renewable resources there, sooner or later you are going to deal with the federal government. Another obstacle is that wind and solar resources produce electricity intermittently. If you are trying to operate a reliable system or run a market system that meets the round-the-clock needs of its customers, you need 24/7 baseload resources as a significant part of the resource mix.

Editor: Explain why renewables-friendly development of our national transmission system is so long in coming.

Shafferman: Wind, solar, and geothermal resources are often in remote areas that are far from the nearest transmission line. We have the dilemma that utility ratepayers don't want to fund new long lines, while renewable project developers, on the other hand, can't

really afford to fund this major expansion of lines and end up having a project that makes sense economically. And as our work for ISO New England has shown us, it is difficult to reach consensus even among various groups of ratepayers about the appropriate allocation of costs. Fortunately, some innovative funding mechanisms have been developed in California – by Southern California Edison and others – that can help build out the grid for renewables.

Editor: What are your thoughts about improving the nation's nuclear capacity?

Shafferman: Nuclear has got to be a significant part of the picture going forward. If big coal plants are environmentally unacceptable, we need clean, replacement baseload plants. As I said before, wind power is intermittent, and thus is not a perfect substitute. The new generation of nuclear plants is demonstrably superior to the past generation of plants and once the steep capital costs are invested, they are cheap to run thereafter.

Editor: You hear stories about how it takes 10 years to bring a nuclear plant online. Isn't that a major stumbling block to bringing more non-fossil fuel generation into our energy-producing portfolio?

Shafferman: The time frame you cite is no exaggeration. However, license applications for a significant number of plants have already been submitted to the Nuclear Regulatory Commission and processing is under way. In addition, federal legislation enacted in 2005 is providing loan guaranty and regulatory risk measures that will encourage nuclear investment.

Editor: What steps can be taken to help build out our transmission system?

Shafferman: A few things would make a real difference. We need a law at the federal level allowing the federal government to handle the siting of all major lines (as FERC does today for interstate gas pipelines), so as to streamline the process for lines crossing multiple states and to avoid resistance due to perceived inequities among those states about relative benefits of those lines. Back in 2005, Congress enacted legislation that went only part way: the federal government had authority over siting only if the state failed to approve a new line within a specific time frame. That didn't really speed things up for crucial new lines.

Also, some innovative and tax-saving ownership structures, like Real Estate Investment Trusts (REITs), could attract new types of investors to fund transmission expansion. Some utilities will consider this approach if the IRS can make it even clearer that this is feasible.

Finally, FERC's continuing use of bonus rates of return for new transmission projects will help spur investment.

Please email the interviewee at hhs@ballardspahr.com with questions about this interview.