Steve Muller's E-Mail to Paul Grant on the Empire Connection, 21 September 2005

Paul,

I am attaching a document containing our last two stories on the Empire Connection project. One announces the failure of the auction process and the other the withdrawal of the project after it was not selected in an RFP for power supply to NYC. I wrote several earlier stories on Empire Connection, but not these last two.

As I mentioned at breakfast today, the merchant transmission concept has had a pretty rough reception in the market. Empire Connection tried to be a true merchant line with open season auctions of transmission capacity. The company attempted to seek long-term capacity commitments from bidders so it could take them to the financial markets and get long-term construction financing based on the stream of revenue from the capacity contracts. The bidders could have been either upstate generators or downstate utilities or energy marketers.

In any case, the auction was not successful. Empire Connection then pinned its hopes on being selected to provide 500 MW of power for NYPA clients in NYC. Empire thought that if it won this RFP, it could get financing for the first phase of the project. However, when NYPA did not select EC, the company threw in the towel.

The two other so-called merchant projects in the US are not true merchant projects in the sense that capacity is autioned regularly. Both the Cross-Sound Cable (in operation between Connecticut and Long Island) and the first phase of the Neptune Project (in construction between New Jersey and Long Island) went through the open season auction process as required by FERC but all the capacity was bought by a single entity, LIPA.

Most other merchant projects are in abeyance. The Pegasus Project is a proposed DC line between Utica, N.Y. and Manhattan via New Jersey. The developer has said that the line brings many advantages to the state and city and should be built as a rate-base project, meaning that the builder gets a fixed rate of return and all grid users pay for the line. This concept is generally the same as that used for the Path 15 expansion in California a year or two ago, but it is controversial in New York.

A couple of other projects have been announced, including one across Chesapeak Bay, one between Alberta and Montana and other between BC and Washington. Only the Alberta one, which is really a short tie line, seems to be going ahead.

One merchant project that might actually have some legs is the Trans-Bay project for San Francisco. This is because of some unique circumstances having to do with the SF market. It is a load pocket and there is a desire to close down several older, polluting plants that currently serve the city, so PG&E is actively looking for replacement power. Meanwhile at the other end of the line are a bunch of IPPs that aren't able to get all their power to market efficiently because of bottlenecks in the existing PG&E grid. I did a story on this; let me know if you would like to see it.

Finally, I should mention a merchant project in Australia that was built but then petitioned to become a regulated investment. Both this project and the Cross-Sound Cable were developed by the same group, Hydro-Quebec/TransEnergie.

I enjoyed your presentations and talking with you at the EPRI conference.

Steve Muller
SNL Energy/Electric Transmission Week

Financiers ready, but investors won't commit to Empire line

March 03, 2004 6:08 PM

By Amanda Jacobson

Long contracts, combined with regulatory and industry uncertainty, contributed to the failure of the Empire Connection transmission auction, according to one industry expert.

On March 1, the *Wall Street Journal* reported that investors, including Kohlberg Kravis Roberts & Co. (KKR), canceled an auction to sell access to the proposed Empire Connection line, which would bring 2,000 MW into New York City. The $700 million Empire Connection project would run along railroads through the New York Power Authority and Consolidated Edison Inc. territories.

Conjunction LLC was developing the project, and the *Journal* reported that investors were "spooked" by market conditions.

James Liles, a regulatory adviser at Milbank Tweed Hadley & McCloy LLP in Washington, DC, and a former FERC staff member, told SNL Financial that "spooked" might not be a good characterization of what happened to the auction participants. The parties involved felt like it was financeable, "but when they went on the Street, they didn't get enough commitment," he said.
In the first attempt at gathering interest for the project, the developers offered 400 MW of capacity in 10-year contracts, Liles said. Buyers were unwilling to sign the long-term contracts due to their inexperience, so the contracts were reduced to five years.

The developers had planned to hold four open seasons for the entire 2,000 MW of capacity, according to Liles, and the recent failed auction was the first leg of that plan.

Liles was unsure whether developers would try to hold another auction, since the most recent attempt already represented a revision from the original 10-year contract offer.

"I don't know what they're planning now," he said. "It is very much on hold right now."

Liles said that FERC regulators were present for the first open season and were probably hoping for a success with the auction. The failure could prompt the FERC to address its policies regarding transmission siting, he said.

The FERC declined to comment for this article.

Liles noted that although the FERC's open season model works well for the gas pipeline industry, it may not work elsewhere because "the merchant power industry is in chaos." Additionally, transmission is far more expensive to hook into the wider system than gas pipelines. And while the FERC has certificate authority to site a gas pipeline, the agency cannot offer this guarantee to transmission developers. Currently, Liles said, FERC regulation is such that developers have to absorb risk and mitigate market power in exchange for being able to charge market prices, but developers and investors could decide that the risk involved is too significant.

"Everybody is thinking this isn't working," Liles said. "People just won't sign up."

Empire Connection will file with FERC to cancel plans for NY transmission line

December 10, 2004 5:09 PM
By Amanda Jacobson

The Empire Connection LLC will file a withdrawal of its plans to build the 125-mile Empire Connection line, according to a docket to be filed with the FERC on Dec. 13.

Empire Connection had held a request for proposals, seeking commitments for 500 MW of transmission capacity to serve New York City. The underground line would have delivered up to 1,000 MW of power to a substation in Queens, according to a Nov. 29 *Electric Transmission Week* report.

James Hoecker and Sara Weinberg, attorneys for Empire Connection, said in a Dec. 9 letter accompanying Empire Connection's withdrawal filing to the FERC: "While the Empire Connection failed to garner the necessary capacity commitments either through an auction, as originally contemplated by the Commission, or through a competitive request for proposal process, Conjunction LLC concludes that the merits of the project from the siting, clean air, reliability, technology, economics, and ratepayer perspectives far exceeded the ability of the current market to sustain such a non-utility effort.

"Notwithstanding the well-recognized deficit in transmission relative to demand that the Nation has experienced in the past decade and one-half and the additional power costs and threats to reliability which electricity 'islands' like New York City must endure (especially if new generation cannot be sited close to load), the 'merchant' alternative to rate-based transmission utility investment currently faces overwhelming obstacles in meeting those challenges," added Hoecker and Weinberg.

The withdrawal is in regard to FERC docket ER03-1353-000.