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Via Email

Michael Judge
Department of Energy Resources
100 Cambridge Street, Suite 1020
Boston, MA 02114

Re: Proposed Amendments to 225 CMR 14

Dear Mr. Judge:

As a practitioner and stakeholder in the Massachusetts renewable energy community with numerous clients undertaking solar projects, I submit the following comments in response to DOER's proposed amendments to portions of 225 CMR 14 (the "Proposed Amendments").

SUMMARY

The Administration is to be commended for its creativity and courage in designing and implementing a market-based solar incentive program aimed at artfully balancing the interests of homeowners, developers, ratepayers, utilities and competitive suppliers while avoiding some of the drawbacks of other solar incentive policy models. DOER's innovative RPS Solar Carve-Out Program has piqued the curiosity of the national solar market and has already led to some impressive results in solar PV installations in the Commonwealth.

At the same time, both within the Commonwealth and around the country, the perceived success or failure of the Administration's innovative Solar RPS Carve-Out Program will turn on whether this summer's "Solar Credit Clearinghouse Auction" (the "Auction") clears and fulfills the Administration's minimum Solar Renewable Energy Certificate ("SREC") price assurance to thousands of homeowners, businesses and developers of all stripes that heeded the Administration's call to invest in solar installations in the Commonwealth.

This is not just a matter of straight talk and fair play. Failure of the Administration's price assurance mechanism could result in real economic harm to homeowners and the failure of commercial solar facilities that have been financed and built with the Administration's price "floor" as a reasonable worst-case assumption.

Just as important, perceived failure of the program will leave millions of dollars of private investment in the Commonwealth on the sidelines and will result in a huge missed opportunity to

gain the confidence of many would-be market participants as the Administration turns to likely development and roll-out of a successor market-based solar incentive program.

The irony here is that this is not a zero sum game where support for the SREC price floor is at the expense of ratepayers, utilities and competitive suppliers. To the contrary, it appears likely that a failed Auction will ultimately result in significantly greater SREC prices and Solar Alternative Compliance Payment (“SACP”) obligations over the life of the current program. In other words, by taking bold steps to ensure a successful Auction, DOER can produce a win-win outcome where over the life of the current program, homeowners, businesses, lenders and investors achieve greater stability in the level of solar incentives and ratepayers, utilities and competitive suppliers achieve valuable moderation in the level of those incentives.

Bold action is needed to ensure that the Auction will clear. Bold actions could include modifying the Proposed Amendments to provide for an even greater and more immediate increase in future SREC purchase obligations in order to provide a more powerful market-clearing incentive. There is apparently a real risk that the more cautious approach embodied in the Proposed Amendments (*i.e.*, merely adding 50,000 SRECs to the CY2013 Compliance Obligation through elimination of the ACP term) will moderate the future negative consequences to purchasers of not clearing this summer’s Auction and therefore make the Auction more – and not less – likely to fail.

A key difficulty that DOER faces is that determining an appropriate course of action requires complex modeling of the SREC market in various scenarios using various assumptions. That exercise is not only complicated but also potentially fraught with the possibility of error. It may prove extremely helpful for DOER, while it is considering comments received during the public comment period, to conduct a public technical session that would allow for in-depth, expert review of that modeling. Should DOER elect not to conduct a technical session, the agency should be all the more wary of proceeding with an approach that may on the surface appear to be cautious but could instead increase the risk of a failed Auction and the risk of higher SREC prices and SACP obligations in the future.

DISCUSSION

The Administration’s Bargain. Until we achieve greater economies of scale, further technological breakthroughs and/or internalize the environmental and health costs of conventional electricity through such means as a carbon tax, investment in solar generation requires incentives. The Solar Carve-Out Program was designed to provide an incentive payment no greater than \$600/MWh and no less than \$285/MWh. This is how DOER advertised its program in a description (downloaded in 2011) aimed at homeowners deciding whether to invest in small solar systems:

DOER has set a ceiling price for SRECs of \$600/MWh, as well as a floor price of \$285/MWh at auction (\$300 minus a \$15 auction fee). As an example of how much revenue may be generated, a 5 kW system would generate an average of 5 or 6 SRECs each year. In most years, these SRECs should sell at prices higher than the \$285/MWh floor price. **However, should you be unable to sell your SRECs by the end of the trading year, you will have the option of depositing them into DOER’s Clearinghouse Auction Account, where they will be sold for a price of \$285 each.**

(Emphasis added.) The catch – not disclosed even in fine print in the program description above – is that the Auction has a fixed net price of \$285 for any SREC sold at the Auction but nobody is actually required to make any bids. This was certainly not intended as a sleight of hand. DOER simply had strong confidence that a broad and ingenious array of regulatory incentives it designed would be sufficient to attract bids and cause the Auction to clear. The problem is that that array of regulatory incentives is currently perceived as being too weak and the somewhat modified incentives currently proposed by DOER are also perceived as being too weak (and may end up actually weakening the original incentives). The market is now oversupplied with SRECs, system owners have been unable to sell their SRECs this year at anything even approaching the “floor” price and so the Auction will be used for the first time this summer. At a recent industry conference, some experts predicted that there will likely be no bidders at all at this summer’s Auction. It is extremely important for the Administration to do everything in its power to ensure that the Auction clears and that all sellers are able to sell deposited SRECs at the \$285 fixed price.

Potential Harm to Massachusetts Homeowners and Businesses. It is difficult to quantify the potential harm in the event that the Auction fails to clear but there are certainly both residential and commercial solar systems installed in reliance on the assurance of \$285/SREC. Homeowners may find themselves unable to pay home equity loans or increased mortgage payments for loans taken out in reliance on expected SREC revenue at \$285/MWh. Commercial solar system owners may find themselves in similar trouble and, if that trouble magnifies and results in economic failure of the project, it could have ripple effects on public entities and other offtakers counting on net metering savings from the project, municipalities counting on increased property taxes, contractors engaged to operate and maintain the project, and so on.

Sidelined Investment. Until the market witnesses a successful Auction as evidence that the price assurance mechanism works, there will be many millions of potential investment dollars on the sidelines and many more resources wasted on projects that never get built and never provide an ongoing economic, grid reliability and environmental benefit. It is now common to have a situation where businesses have invested significant resources in securing project sites, obtaining permits, struggling through the long and costly utility interconnection review process, and negotiating agreements to sell power or net metering credits – only to have “shovel ready” solar projects on indefinite hold because a lender is nervous about whether the Auction will work to support the \$285/MWh floor or the business cannot find a so-called “SREC investor” in the market (typically a market speculator of some sort that is placing bets on multiple SREC markets across the county). Bold action to ensure that the Auction clears will get that investment off the sidelines, and wrapping up the Administration’s current 400 MW program on that sort of positive, energized note could also serve as a tremendous boost to promote the post-400 MW successor program that DOER is currently starting to design.

Ratepayer Protection. DOER deserves credit for designing and implementing an innovative incentive program that balances incentives for solar development against the need to protect ratepayers from providing undue subsidies. The program was designed to make homeowner and businesses bear the risk that the SREC incentive would be anywhere between the ceiling price and the floor price. If the program worked to drive the SREC incentive down to \$285/MWh, that would be a huge victory for ratepayers. In fact, the program has worked to drive the SREC incentive down but ratepayers have effectively been overprotected in the near-term – and the

price assurance to homeowners and business breached – as uncertainty about the integrity of the Auction has driven SREC prices around \$200/MWh for much of the last year. But low near-term SREC prices will drive sellers to deposit SRECs in the Auction and, if the Auction fails to clear, the regulations provide that SREC purchase requirements will ratchet up in future years and that is expected to cause undersupply, SREC prices well above the floor and SACP obligations, all to the long-term detriment of ratepayers, the utilities and competitive suppliers.

Alternative, Bolder Auction-Clearing Mechanisms. DOER should consider modifying the Proposed Amendments to include one or more bolder auction-clearing mechanisms. Promising ideas along those lines include:

- increase the 2013 Compliance Obligation by 100,000 SRECs instead of 50,000 SRECs;¹
- add to the CY+2 Compliance Obligation two times the number of deposited SRECs in the event that the 3rd round of the Auction fails to clear (in addition to the one times adjustment that would have already been made in connection with the mere deposit of SRECs into the Auction);
- create a 4th round of the Auction in which SRECs are given an additional year of extended life;
- if a 4th round of the Auction is created and fails to clear, add to the CY+2 Compliance Obligation two times the number of deposited SRECs

The specific mechanisms are less important than the overall objectives: causing this summer's Auction to clear and avoiding modifications to the program that, as tested through careful modeling, carry a significant risk of weakening incentives for the Auction to clear.

In weighing whether to proceed with the Proposed Amendments, with or without modifications, DOER should certainly carefully consider the concerns of developers and SREC investors that believe they have a vested interest in the current regulations and that it would be inequitable to changes the rules in the middle of the game. At the same time, it will make sense for DOER to consider whether any particular amendment does or does not undermine the reasonable expectations of market participants. A market participant may have invested in the SREC market expecting that SREC sellers and/or purchasers will act rationally with an awareness of how the regulations function. Such expectations seem reasonable and regulatory changes that upset them may not be fair. On the other hand, a market participant may have invested in the SREC market betting on the possibility that SREC sellers and/or purchasers will not act rationally. Such expectations may not be reasonable and regulatory changes that are designed to discourage irrational behavior and reinforce rational, enlightened behavior may be entirely fair.

Need for Technical Session. It is difficult for stakeholders to comment on the Proposed Amendments or propose alternative approaches without having some common understanding with DOER about impacts on the SREC market in various scenarios and under various assumptions. Boosting the 2013 CY Compliance Obligation through elimination of the ACP term may be an excellent idea that is unlikely to have unintended consequences but it also seems as if that change would well have unintended consequences if the number of SRECs deposited in

¹ Although this change might impose the largest near-term burden on competitive suppliers in the middle of the 2013 Compliance Year, competitive suppliers also have a great deal to gain by moderating or eliminating undersupply in future years.

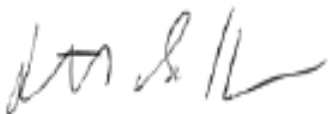
the Auction is smaller and results in a planned boost to future year Compliance Obligations that is also smaller and fails to operate as enough of a negative consequence to cause this summer's Auction to clear. If that were the case, it may be better to make no change to the Compliance Obligation formula than to make a modest change. Conducting an in-depth public technical session could help both DOER and stakeholders more fully vet alternative approaches against the range of likely outcomes.

Elimination of Opt-in Term Reduction. There is currently a 10-year Opt-in Term in which SREC-qualified facilities can deposit unsold SRECs into the Auction but the current RPS regulations call for an automatic reduction in the length of the Opt-in Term when significant numbers of SRECs are deposited into the Auction. Based on current data, it appears certain that mechanism will result in a reduction of the Opt-in Term from 10 years to 8 years effective for facilities that qualify for the Solar Carve-Out Program on or after July 20, 2013. It took a good deal of time after the program was established to get financing parties comfortable with the program. There are many financing parties that still have no appetite for the Massachusetts solar market in the absence of much greater assurance of the price "floor" in the program. Those financing parties that have made an uneasy peace with the program have developed terms, conditions and practices around the 10-year Opt-in Term, generally allowing amortization of loan costs over the 10-year Opt-in Term. Shortening the Opt-in Term would cause a domino effect that would increase borrowing costs and potentially make some solar projects unfinanceable.

DOER should examine very closely the benefits of retaining the automatic Opt-in Term adjustment provision against the benefits of eliminating it. The key justification for reducing the Opt-in Term is to dampen new supply of SRECs and cool off an overheated SREC market. By dampening supply, it is possible to support SREC market prices without relying wholly on increasing regulatory demand. But market observations suggest that the impending Opt-in Term reduction may be having the opposite effect of the one intended by encouraging developers to accelerate project development and obtain a Statement of Qualification prior to the reduction date. Eliminating Opt-in Term reductions may prove to be more beneficial in light of the Administration's policy objectives. Preserving a 10-year Opt-in Term would be the best means of leveraging the hard-won solar financing practices that have grown around the current Opt-in Term. Reducing the Opt-in Term might help to support SREC prices but it would be next to impossible for market participants to predict how the reduction would affect future supply. For that reason, reducing the Opt-in Term could actually make it more difficult for compliance formula adjustment to send unambiguous signals to the market to force the Auction to clear.

Thank you very much for the opportunity to provide these comments and for your consideration.

Sincerely,



Jonathan Klavens