

SOUTH DAKOTA PUBLIC UTILITIES COMMISSION

CASE NO. EL05-022

IN THE MATTER OF THE APPLICATION BY OTTER TAIL POWER COMPANY

ON BEHALF OF THE BIG STONE II CO-OWNERS

FOR AN ENERGY CONVERSION FACILITY SITING PERMIT FOR THE

CONSTRUCTION OF THE BIG STONE II PROJECT

PREFILED REBUTTAL TESTIMONY

OF

THOMAS A. HEWSON, JR.

PRINCIPAL

ENERGY VENTURES ANALYSIS, INC.

JUNE 16, 2006



1 **BEFORE THE SOUTH DAKOTA PUBLIC UTILITIES COMMISSION**
2 **PREFILED REBUTTAL TESTIMONY OF THOMAS A. HEWSON, JR.**

3
4 **Q: Please state your name.**

5 A: My name is Thomas A Hewson, Jr.

6 **Q: On whose behalf are you submitting testimony?**

7 A: The proponents of Big Stone Unit II (the "Applicants").

8 **Q: How are you currently employed?**

9 A: I am a principal at Energy Ventures Analysis, Inc. ("EVA"), an energy consulting firm
10 located at 1901 North Moore Street in Arlington Virginia.

11 **Q: At page 18, lines 20-24, of their May 26, 2006 testimony, Mr. Schlissel and Ms.**
12 **Sommer testify that it is reasonable to assume that the production tax credit for wind**
13 **facilities will be extended before it expires at the end of 2007. Do you agree?**

14 A: No, based on past experience, I do not think it is reasonable to assume the production tax
15 credit will be extended before it expires at the end of 2007. More importantly, I do not think it is
16 reasonable to assume that, even if the tax credit is extended at the end of 2007, the tax will be
17 extended over the long term. I am not expressing a view on whether the tax credit should or
18 should not be extended. I am simply saying that, for planning purposes, it cannot be assumed
19 that it necessarily will.

20 **Q: On what do you base these conclusions?**

21 A: The tax credit has been extended by Congress on four occasions, but on three of those
22 occasions Congress let the tax credit lapse before extending it. The tax credit was originally

1 enacted as a part of the Energy Policy Act of 1992 and expired on June 30, 1999. The tax credit
2 was not restored until December of 1999, when Congress extended it until December 31, 2001.
3 The tax credit then lapsed again until March 2002, when Congress extended it through December
4 31, 2003. The tax credit then lapsed again for about eight months until November 2004 when
5 Congress again extended it through December 31, 2005. In the Energy Policy Act of 2005,
6 enacted last summer, Congress for the first time extended the tax credit without first having let it
7 lapse, this time until December 31, 2007. As the American Wind Energy Association (AWEA),
8 the principal lobbying arm of the wind industry, stated in a July 29, 2005 press release following
9 Congress' most recent extension of the tax credit, "[t]his is the first time that an extension of the
10 production tax credit for wind energy has been approved before the credit expires, and, following
11 the past six years of boom-and-bust cycles caused by successive expirations, that is very good
12 news for the industry." This history does not give me a great deal of confidence that Congress
13 will timely extend the tax credit before it expires at the end of next year.

14 **Q: Do you think it is reasonable to assume that Congress will extend the tax credit over**
15 **the long-term?**

16 A: No. In the first place, Congress has never granted a long-term extension of the tax credit,
17 and instead has only been willing to grant successive two-year extensions. It has taken these
18 actions despite the position taken by wind advocates that a long-term tax credit is needed in the
19 industry to foster wind development.

20 In addition, a major justification for the tax credit was to increase wind generation by
21 offsetting wind's higher production costs. It has been thought that, eventually, increased turbine
22 demand would result in technology improvements that would make wind more cost-competitive

1 versus conventional generation alternatives. This objective has been reached, at least according
2 to wind industry claims.

3 Promoting wind production has also been accomplished through renewable portfolio
4 standards (RPS) in 23 states that set aside a portion of the retail demand that can be met only
5 through use of qualifying renewable energy options. Overall, the RPSs already enacted have set-
6 aside 250 TWh by 2030.

7 This combination of wind energy advocates' assertions that wind is achieving more
8 competitive costs and a protected set-aside market share may be sufficient for Congress to
9 conclude that its goals of promoting and encouraging wind power production have been met and
10 that no further future federal subsidies are required. In addition, long-term budgetary concerns
11 may cause Congress to conclude that the tax credit should no longer be extended.

12 **Q: How significant is the production tax credit issue to Mr. Schlissel's and**
13 **Ms. Sommer's testimony?**

14 A: Quite significant. Their testimony makes two predictions as to future Congressional
15 action that would affect the cost-competitiveness of the Big Stone Unit II station. First, they
16 state that they believe that Congress will adopt carbon dioxide controls that will have a
17 compliance cost of \$19.10/ ton CO₂. See their May 19, 2006 testimony, p.18. Their testimony
18 translates this cost into a levelized cost impact of \$18.61/MWh to the disadvantage of coal
19 generation. See their May 19, 2006 testimony, page 23, Table 4. Second, they state that they
20 believe Congress will continue to extend the production tax credit for wind. They state that the
21 tax credit has a cost impact in favor of wind generation of \$12, \$21, \$23, or even \$28/MWh,
22 depending on various assumptions. I have not personally checked any of these numbers and do

1 not vouch for them. However, assuming Schlisel and Sommer's numbers are correct, it seems to
 2 me that if they are wrong on one of their two forecasts of future legislative action, the effect
 3 would be to essentially cancel the other out. In other words, if the production tax credit is not
 4 extended, the cost impact on the wind industry would cancel out the advantage they would
 5 receive by Congress' enactment of CO2 legislation of the character Schlissel and Sommer
 6 forecast.

7 In addition, although (as noted) wind advocates often say that wind is now cost-
 8 competitive with other resources, in lobbying Congress for extensions of the production tax
 9 credit, they frequently complain that lapses in reauthorization of the credit have had a deleterious
 10 impact on the industry. For instance, an October 28, 2004 AWEA press release noted "[t]he
 11 slow-down in installations in 2004 that resulted from the expiration of the production tax credit"
 12 at the end of 2003. In a September 24, 2004 press release, AWEA called the tax credit "a critical
 13 factor in financing new wind power installations." In a November 25, 2003 press release,
 14 AWEA stated that "[i]t is impossible for the U.S. wind industry to maintain a steady growth rate
 15 in the present climate of uncertainty." Similarly, according to the Union of Concerned
 16 Scientists,

17 "Unfortunately, the continuing 'on-again/off-again' game being played with the PTC
 18 by Congress has contributed to a boom-bust cycle of development that is plaguing the
 19 wind industry The cycle begins with the wind industry experiencing strong
 20 growth in development around the country during the years leading up to the PTC's
 21 expiration. Lapses in the PTC then cause a dramatic slow down in the
 22 implementation of planned wind projects. When the PTC is restored, the wind power
 23 industry takes time to regain its footing, and then experiences strong growth until the
 24 tax credits expire. And so on."¹
 25

¹ http://www.ucsusa.org/clean_energy/clean_energy_policies/production-tax-credit-for-renewable-energy.html
 (Page Last Revised: 04/13/06).

1 In sum, it should not be assumed that the production tax credit will be extended again in
2 2007 for the long-term. Congress' failure to do that could have a very significant impact on the
3 relative economics of wind and coal.

4 **Q: Does this conclude your testimony?**

5 **A:** Yes.

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