

United States Department of the Interior

OFFICE OF THE SECRETARY Washington, DC 20240

MAY - 6 2013

The Honorable Lamar Alexander United States Senate Washington, D.C. 20510

Dear Senator Alexander:

Thank you for your letter dated November 9, 2012, cosigned by Senator David Vitter, regarding the Department of the Interior's announcement of the first commercial lease for renewable energy under the 'Smart from the Start' initiative. Secretary Jewell has asked me to respond to your letter. A similar response has been sent to Senator Vitter.

Renewable energy development, including offshore wind projects, promotes the Administration's all-of-the-above energy strategy by expanding domestic energy production and creating jobs. As proposed, the NRG Bluewater Wind project would provide enough electricity to power more than 100,000 homes, and would support new construction and operations jobs.

Please see the enclosed document prepared by the Bureau of Ocean Energy Management (BOEM), which provides specific responses to the six issues you raised in your letter.

I look forward to working with you to promote an all-of-the-above strategy to expand safe and responsible domestic energy production.

Sincerely,

Tommy P. Beaudreau

Acting Assistant Secretary – Land and Minerals

Management

Enclosure

Bureau of Ocean Energy Management (BOEM) Responses to Questions from Senator Vitter and Senator Alexander November 09, 2012

1. The Federal Government derives significant revenue from royalties for offshore oil and gas production on top of substantial up-front competitive bids for the rights to explore and produce energy (these bids alone totaled nearly \$10 billion in FY 2008). The current royalty rate companies must pay is between 12.5 percent and 18.75 percent. This, when combined with bonus bids, constitutes a substantial tax right on all energy produced by an oil and gas company working on federal offshore or onshore resources. What is the effective royalty rate Interior has contracted with NRG Bluewater Wind Delaware LLC for this lease for the energy it produces? What is the anticipated revenue to be raised from this development over the next 10 years?

Response: A royalty rate, as it relates to Outer Continental Shelf (OCS) oil and gas production, is applied to actual net product sales revenue to determine the royalty obligation of the lessee to the government. Net product sales revenue represents actual sales value less transportation costs. In contrast, the Department of the Interior (Department) contracted with NRG Bluewater Wind Delaware LLC (NRG) for it to pay an operating fee rate of 2 percent through the first eight years of commercial operations, and 4 percent thereafter. The operating fee rate is applied to a prospective measure of sales value, i.e., the anticipated sales value of electricity generation in the coming year. The anticipated sales value to which the operating fee is applied is based on the recent average spot wholesale market price of electricity in the region adjacent to the project. The operating fee is calculated as the product of the operating fee rate and the anticipated wholesale market value of electric generation in an upcoming year. During the first 10 years of the lease, we project operating fees to be about \$10.4 million and rentals to be about \$1.5 million. NRG has already paid an acquisition fee of about \$24,000.

The Department has adopted acquisition, rental, and operating fees for wind projects that are lower than those it charges for oil and natural gas lease rights on the OCS in part because wind energy projects do not use a depletable resource. The lower offshore wind operating fee relative to OCS oil and gas royalties also reflects other differences such as the maturity of each industry.

2. If NRG Bluewater Wind Delaware LLC received the wind energy production tax credit (currently a 2.2 cents per kilowatt hour payment regardless of demand at the time of production) does the contract stipulate that the royalty rate be adjusted to ensure there won't be a net payout of federal tax dollars to NRG Bluewater Wind Delaware LLC? In other words, will this company get paid by the federal government to produce wind energy so they can in turn pay any royalty they might owe to the federal government? Will the total value of any production or other renewable tax credits exceed the price paid for the lease?

Response: The contract with NRG does not stipulate that the operating fee will be adjusted during the life of the contract based on receipt by NRG of the production tax credit (PTC). However, the contract does specify that the operating fee will increase from 2 percent to 4 percent beginning in year nine of commercial operations. Generally, the PTC plays an important

part in attracting investor financing for large scale renewable energy projects that require substantial up-front capital expenditures.¹ These investors are often represented by large institutional financial firms and their customers who are a significant source of financing for wind energy projects.² With this lease NRG has the potential to build one of the first offshore wind farms in the United States. Due to the many uncertainties in the nascent offshore wind industry, including transmission capacity, wind farm siting and generation capacity, and future energy prices, the PTC is often important to providing some certainty to project investors and may serve as a means to lower the effective installed costs of wind energy capacity by a significant portion.³ The PTC currently provides a 2.2 cent per kilowatt hour payment for the first 10 years of power generation from renewable energy commercial operations.

3. In Interior's November 23, 2010, press release for the "Smart from the Start" initiative, it was indicated that "a revision to its regulations that will simplify the leasing process for offshore wind in situations where there is only one qualified and interested developer" was in our national interest. Given that there was no competitive bidding for this lease, what was the actual bid for this lease, and how does that compare to the average bonus bid that was paid in the last OCS lease sale for an oil and gas lease on equivalent acreage?

Response: The Cash Bonus and/or Acquisition Fee paid by NRG for the lease was \$0.25 per acre, amounting to \$24,107.50 for the 96,470 acres. The average bid per acre for the last oil and gas lease sale held on November 28, 2012, in the western Gulf of Mexico, was \$205. However the two amounts cannot be appropriately compared since a) the Delaware wind energy lease sale was based on an acquisition rate deemed fair and appropriate specifically for renewable energy uses, while the oil and gas leases are offered under a regime tailored to oil and gas in the particular region and operating environment (for example, the minimum bid price for OCS oil and gas leases in the Gulf of Mexico shallow water is \$25 per acre and \$100 for deepwater leases), and b) the resources underlying the bids have fundamentally different values as partly reflected in their minimum required bid and acquisition prices.

Moreover, renewable energy projects do not use a depletable resource, but they do occupy public land to the exclusion of other potential uses. Therefore, the Department has adopted acquisition, rental, and operating fees for access to wind energy that are lower than those charged for the rights to offshore oil and natural gas resources for extraction on the OCS.

4. Who are the intended customers for the electricity to be sold by NRG Bluewater Wind Delaware LLC, and what rate have they indicated they will be able to charge utilities for bringing electricity on to the grid? After all, according to the Energy Information Administration, offshore wind generation is estimated to be over three times as expensive to build and operate as onshore wind generation.

¹ Wiser, R., B. Mark, G. Barbose. 2007. Ernest Orlando Lawrence Berkeley National Laboratory. *Using the Federal Production Tax Credit to Build a Durable Market for Wind Power in the United States*: http://eetd.lbl.gov/ea/emp/reports/63583.pdf

² United States International Trade Commission. 2009. http://www.usitc.gov/publications/332/ITS-2.pdf
³ Wiser, R., B. Mark, G. Barbose. 2007. Ernest Orlando Lawrence Berkeley National Laboratory. *Using the Federal Production Tax Credit to Build a Durable Market for Wind Power in the United States*: http://eetd.lbl.gov/ea/emp/reports/63583.pdf

Response: Issues related to rates and power purchase agreements are commercial considerations for project proponents, utilities, states, and localities. However, we are aware that the Cape Wind project offshore Massachusetts currently has power purchase agreements in place for approximately 75% of the project's anticipated power generation capacity.

5. What utility companies have indicated they are interested in purchasing electricity from NRG Bluewater Wind Delaware LLC, and what states are within the potential service area where consumers will be paying the additional costs of this electricity?

Response: See response to question #4 above.

6. What has been the environmental review process in awarding NRG Bluewater Wind Delaware LLC this lease? Did this process take into consideration threats posed by the development to avian species that could be impacted by wind turbines?

Response: BOEM published the Mid-Atlantic Final Environmental Assessment (EA) in February 2012, to inform decisions on whether to issue a lease in the Delaware Wind Energy Area (WEA), and to subsequently approve Site Assessment Plans (SAPs) on the lease. The EA considered whether (1) issuing leases, and (2) approving site assessment activities in a certain area of the OCS offshore Delaware would lead to reasonably foreseeable significant environmental impacts, and thus, whether an environmental impact statement (EIS) must be prepared before a lease was issued. Upon the completion of the EA, BOEM concluded that issuing a lease and approving site assessment activities within the Delaware WEA would have no significant impact on the environment. As a result, the preparation of an EIS was not necessary for BOEM to proceed with the lease issuance process with NRG.

Once NRG submits a SAP, BOEM would determine whether the Mid-Atlantic EA adequately considers the environmental consequences of the activities proposed in NRG's SAP. If BOEM determines that the analysis in the EA adequately considers the consequences, then no further NEPA analysis would be required before the SAP is approved. If, on the other hand, BOEM determines that the analysis in the EA is inadequate for that purpose, BOEM would prepare an additional NEPA analysis before considering approving the SAP.

Per the Mid-Atlantic Final EA and the Finding of No Significant Impact (FONSI) 2012, BOEM concluded that avian species may be affected by vessel discharge; the presence of meteorological towers and buoys, and accidental fuel releases. However these impacts were determined to be negligible to minor and activities and events associated with leasing the entire WEA pose no threat of significant impacts to these animals. The EA did not analyze the potential impacts to avian species related to wind turbines. If and when NRG is prepared to propose wind energy generation on its lease, it will submit a Construction and Operation Plan (COP). If a COP is submitted, BOEM would prepare a site- and project-specific NEPA analysis.

In addition, BOEM has an environmental studies program that develops, conducts and oversees scientific research specifically to inform policy decisions regarding development of OCS energy

and mineral resources. The BOEM currently has several ongoing studies focused on developing further understanding of the potential impacts on avian species from wind energy development.



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