ELECTRIC POWER RESEARCH INSTITUTE

Collaborative EPRI Analysis of CO_2 Price Impacts on Western Power Markets:

Preliminary Results for Discussion

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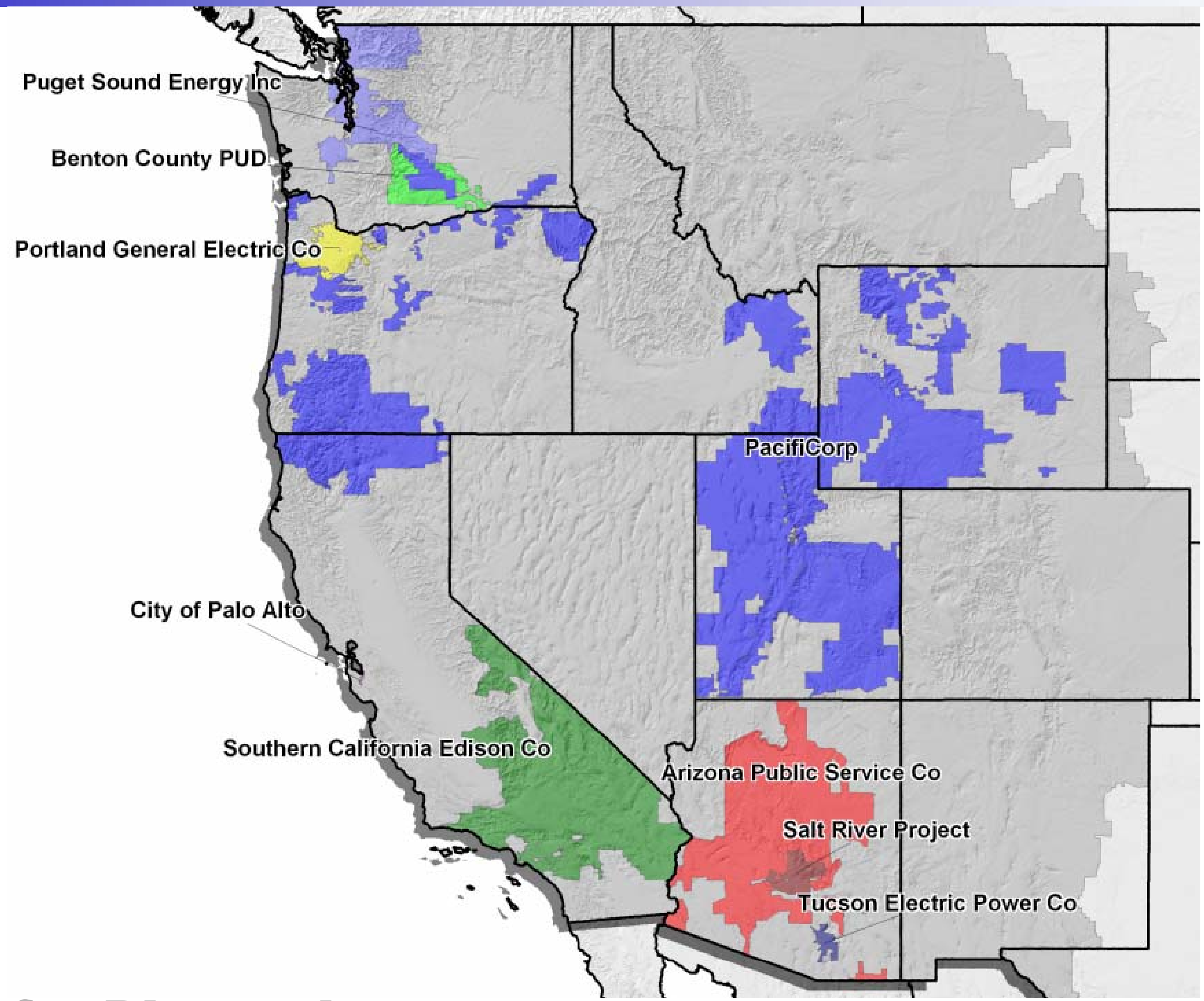
Webcast Background

- Been working with 9 utilities to examine impact of CO_2 price on WECC power markets and emissions
- Have lots of exciting results to share
- Dealing w. complex issues so results are preliminary and feedback is welcome
- Repeat/follow-up Webcast expected week of June 23rd

WECC Collaborative Overview

- Many proposals at national level to regulate CO_2
- Project extends Coal/Gas-Land analysis to WECC market
- Adapts methodology to unique features of WECC
- Goal is to conduct a broad-brush, indicative assessment of the effects of CO_2 price on WECC power markets and electric sector over time
  - Power prices
  - CO_2 emissions
  - Generation demand for natural gas
  - Cash flows to generation categories
- Effects on overall economy not covered
- Collaborative effort by diverse set of nine companies

WECC and Participating Companies



Study is EPRI Product

- **This is an EPRI analysis** - focuses on CO_2 price impacts on western power market through 2030
- **The Base Case is not a forecast** - rather a point of reference for gaining insights about how climate price would impact power markets, customers, and emissions
- **The results are highly sensitive to input assumptions so numerous sensitivity cases were examined**
- **Preliminary results reflect EPRI's best estimates at this point** - and do not necessarily reflect the views of the project participants
- **This report should be viewed as a interim step in an ongoing voyage of discovery** – feedback and comments from all parties are welcome

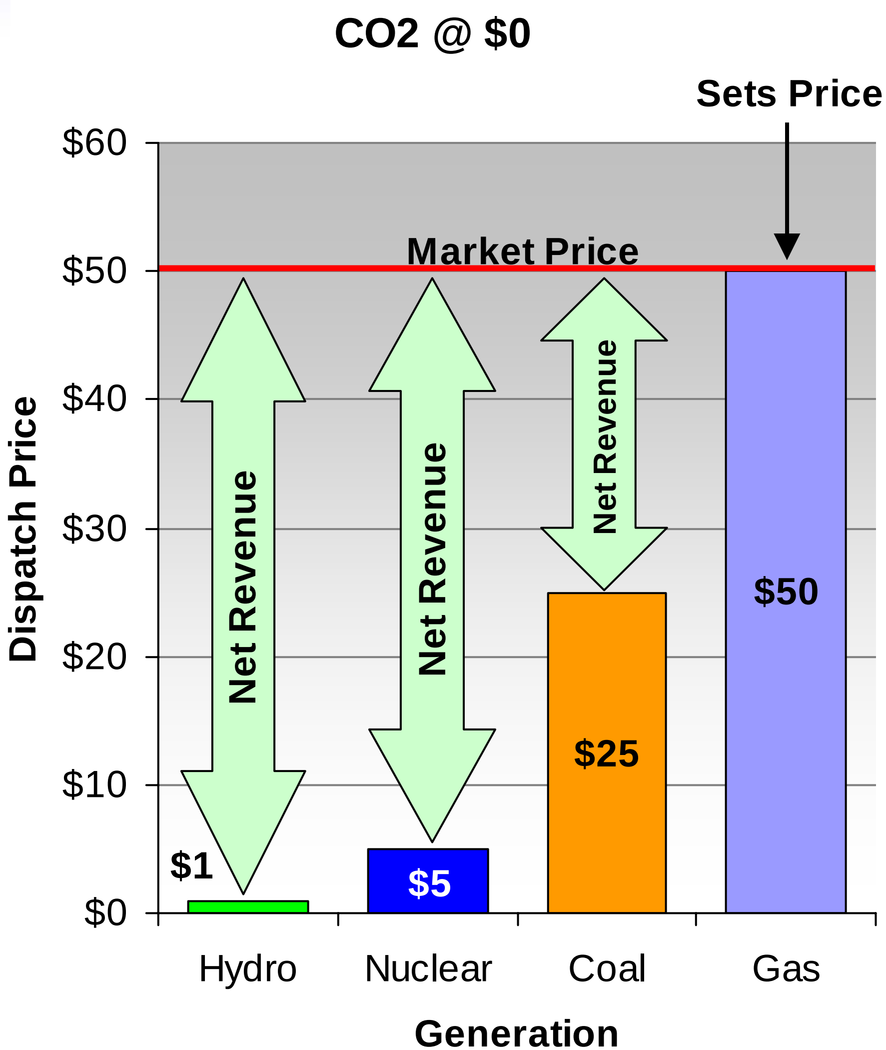
Summary of Key WECC Assumptions

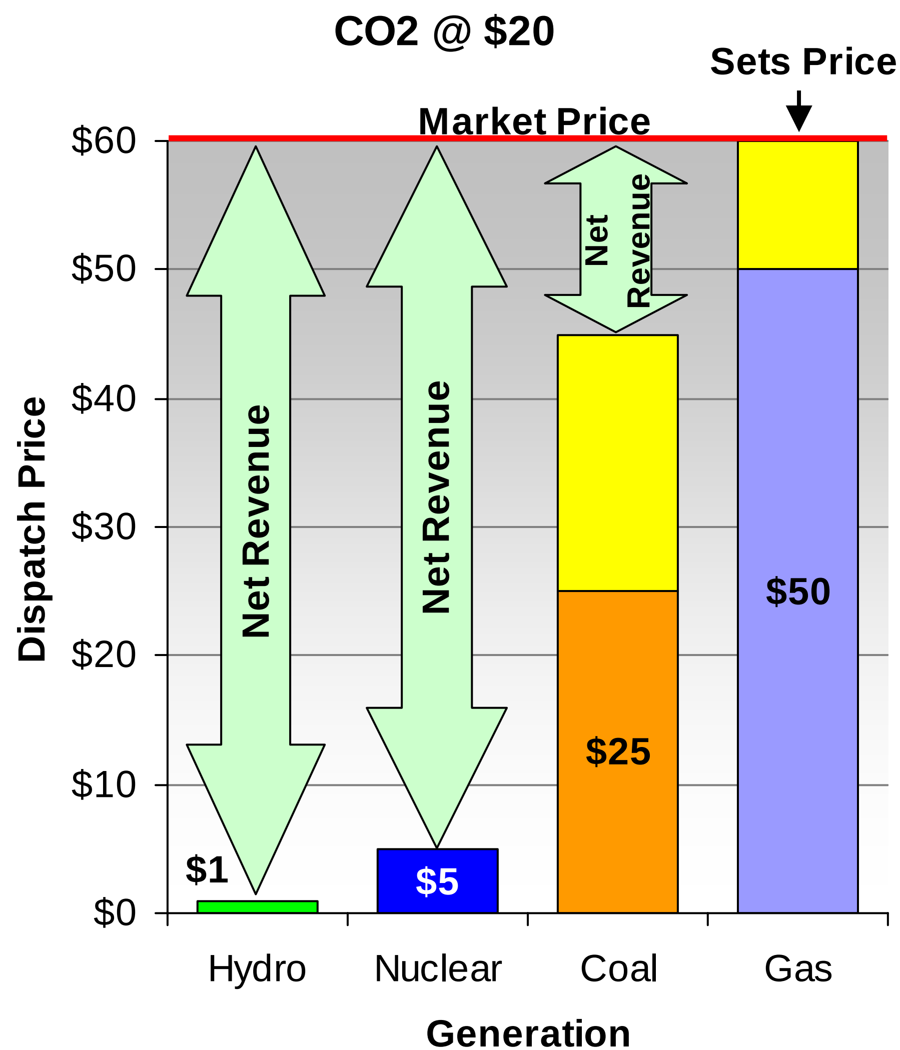
- Model and data update
  - Calibration to 2006 actual data
- Hydro capacity and generation
  - ~200 TWh in 2006, remains flat in the future
- Load growth and elasticity assumptions
  - Load grows at 1.73%/year; elasticity assumed at -0.5 long-term
- Fuel and capital costs
  - Gas in real 2006 dollars; pegged to 5/6 NYMEX
  - Capital examples: Coal ($2850/kW); Nuclear ($4350); Renewables ($2820)
- Renewables assumptions
  - RPS targets are assumed met as baseline
- Timing assumptions for technology introductions
  - Nuclear constraint pre-2019
  - Only "on-the-shelf" technologies are assumed deployable

CO_2 Policy Can Have a Dramatic Impact on Generation Costs, Power Prices, and Cash Flows

- Each dollar of CO_2 value boosts fossil dispatch costs
  - ~ $1.00/MWh for coal-fired generation
  - ~ $0.40/MWh for gas-fired CC
  - ~ $0.60/MWh for gas-fired CT/boiler
- Present value of $10/ton CO_2 payments for coal-fired plant approximately equal to half of plant investment cost
- But higher dispatch costs mean **higher power prices**
- Net impact on cash flow depends on net balance of cost impacts against net revenue impacts from a CO_2 price

CO_2 Price Impacts Electric Market Price and Generator Net Revenue for Each Hour of Dispatch





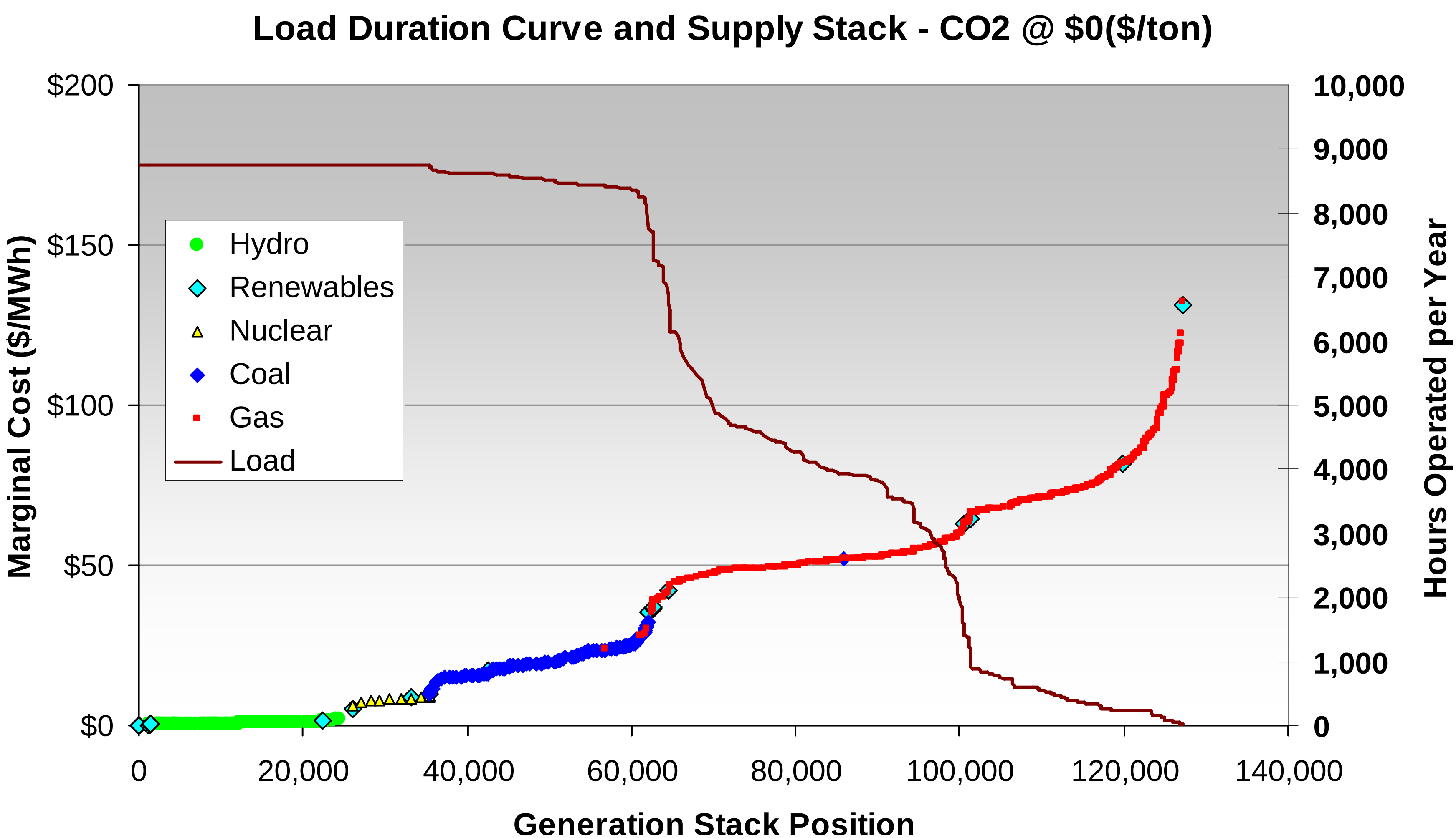
Modeling System Integrates All Major Options for Reducing Electric Sector CO_2 Emissions

- Combines three CO_2 reduction activities for generation in integrated cost-minimizing mix
  - Redispatch existing generation (short term effect)
  - Add new generation to cover growth and retirements (long term effect)
  - Substitute new generation to cut existing source emissions (long term effect)
- Reflects lead times to build new capacity
- Does not incorporate detailed system constraints on operations, transmission or new investment
- Includes role of customer load response to higher power prices (and the interaction over time with needs for new generation)

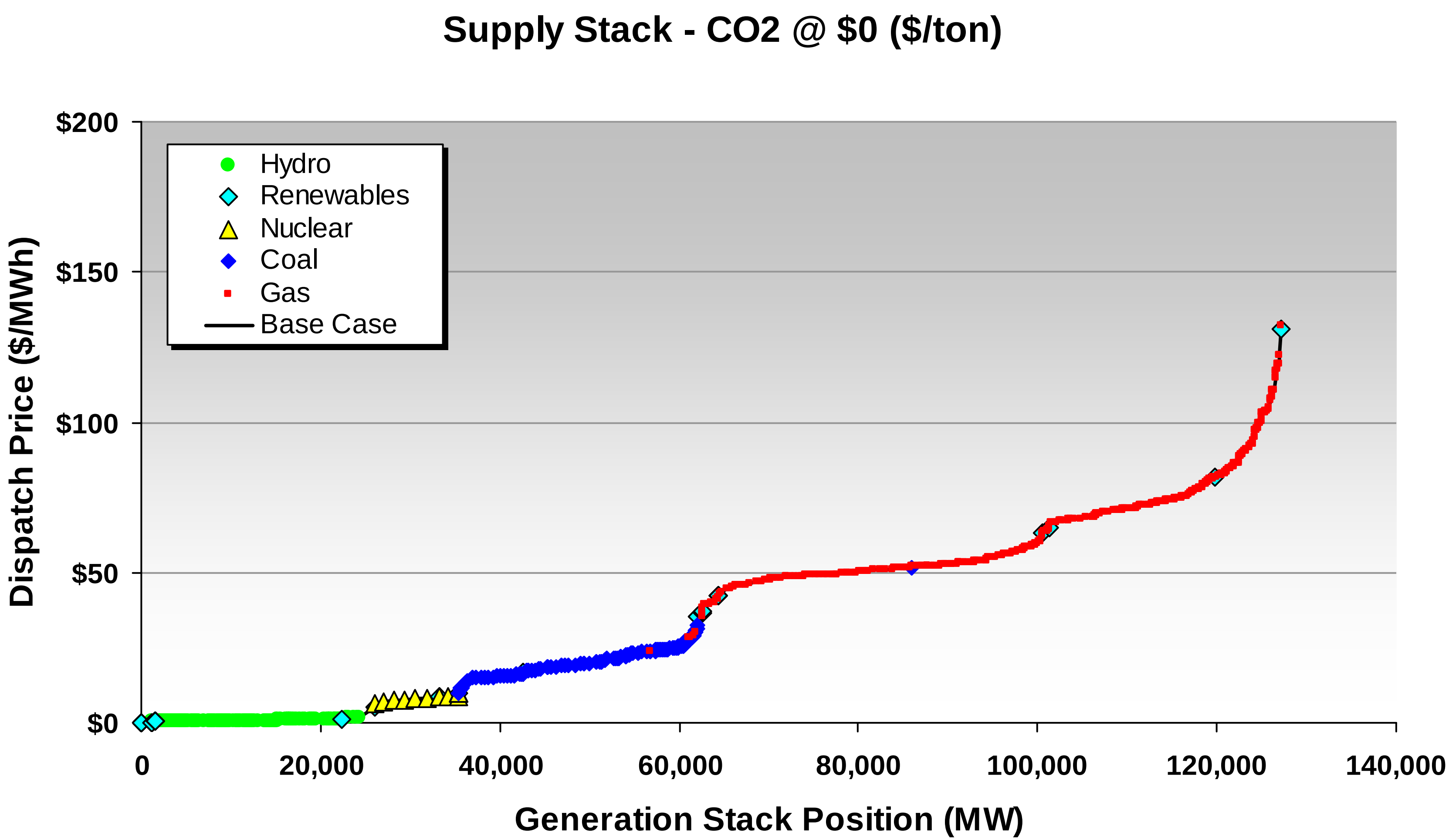
Analysis is Based on Market Model of Behavior

- Tracks impacts of a range of CO_2 prices on the power market
  - Price scenarios reveal impacts on power sector, but are not meant to model specific tax or cap & trade policies
  - Allowance allocation is not addressed
    - Not expected to affect prices in a competitive market
    - Not expected to affect incentives for investment
- Expects competitive market behavior to continue
  - Systems operate to minimize cost, maximize value
  - Add new generation only if cost can be recovered

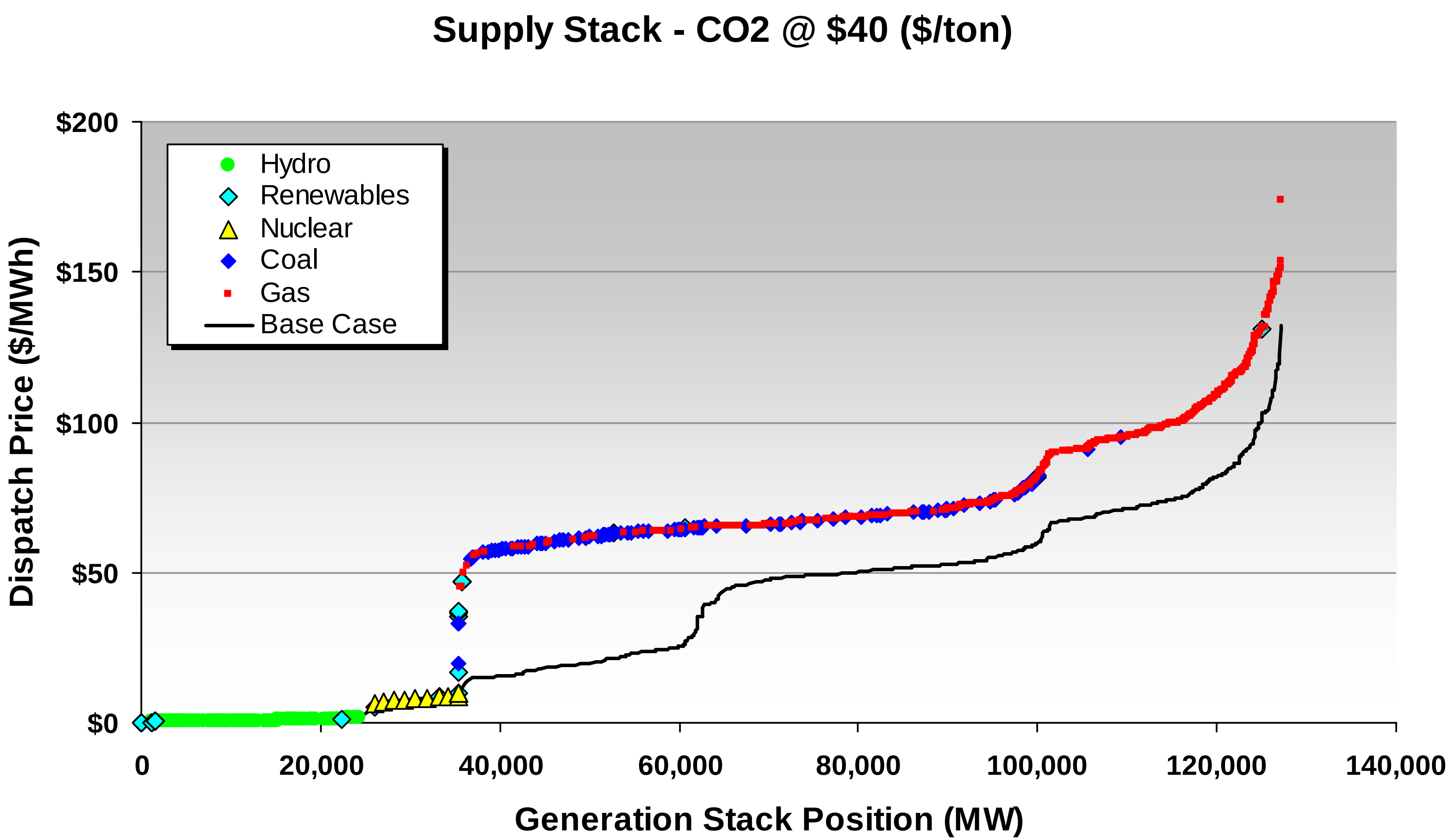
Supply Stack and Load Duration Curve Capture Operation of the System Each Year



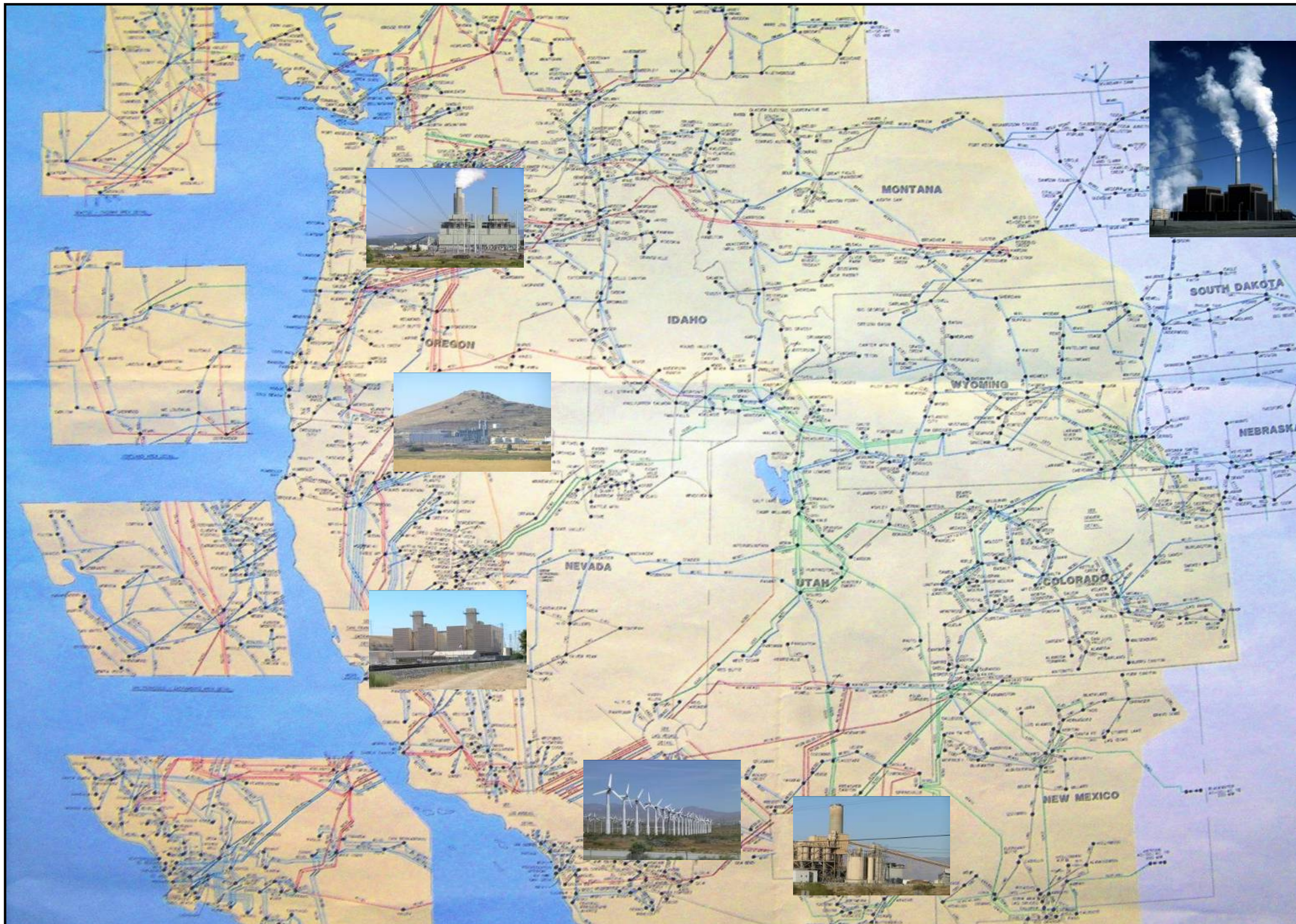
What Happens When CO_2 Has a Price? – $0/ton



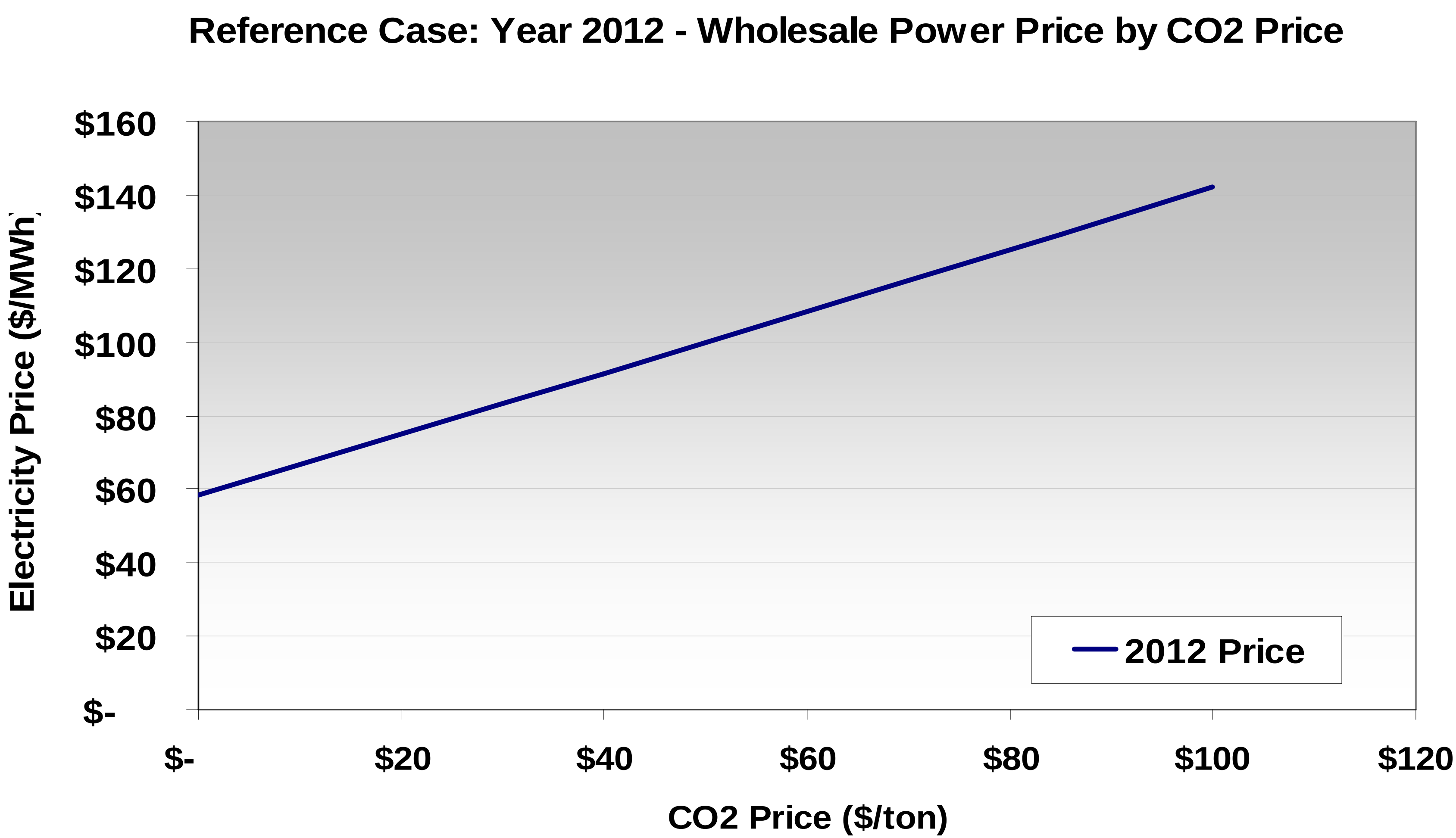
What Happens When CO_2 Has a Price? – $40/ton



Analysis Results

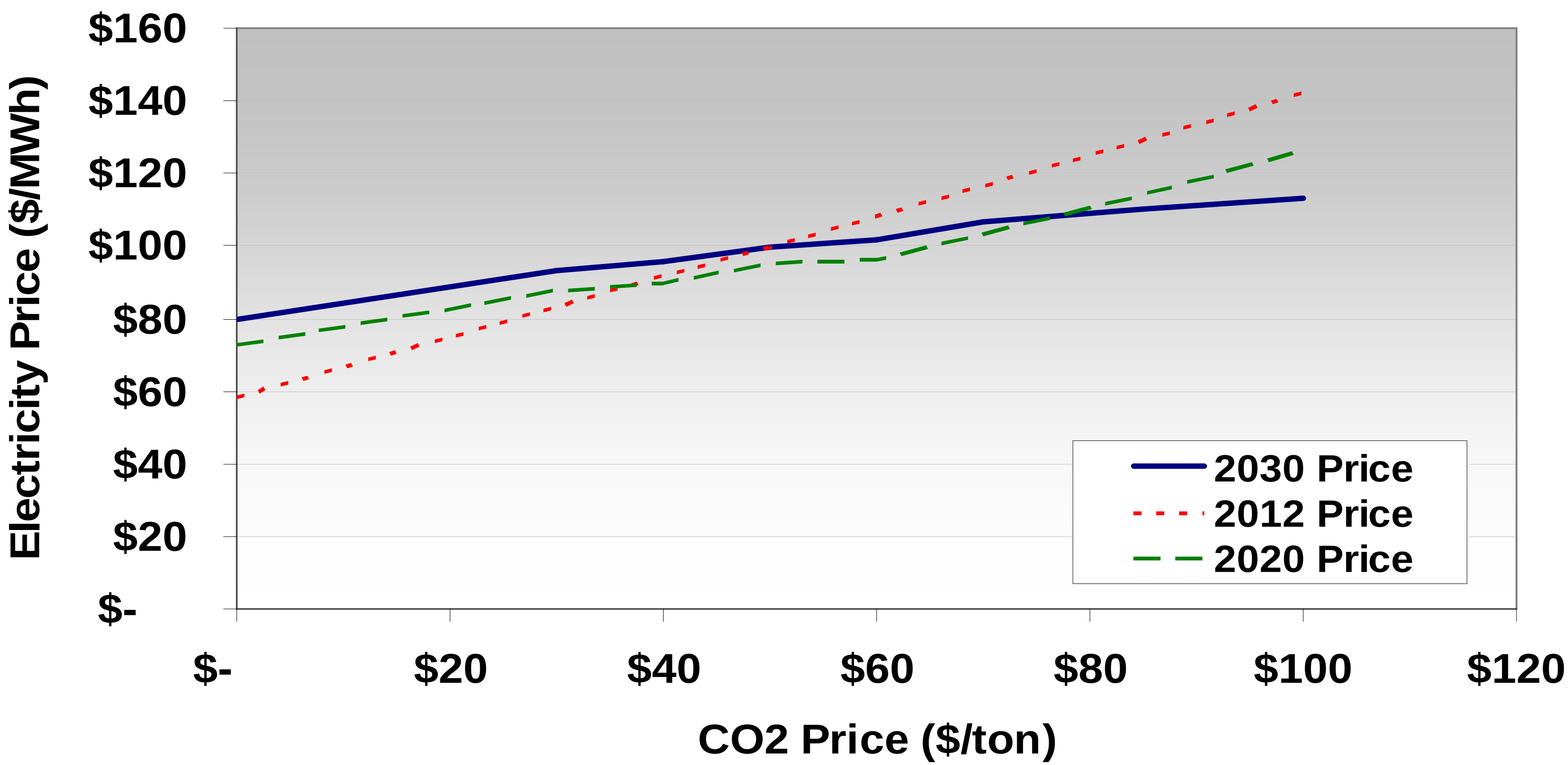


Impact of CO_2 Price on Wholesale Power Prices - 2012

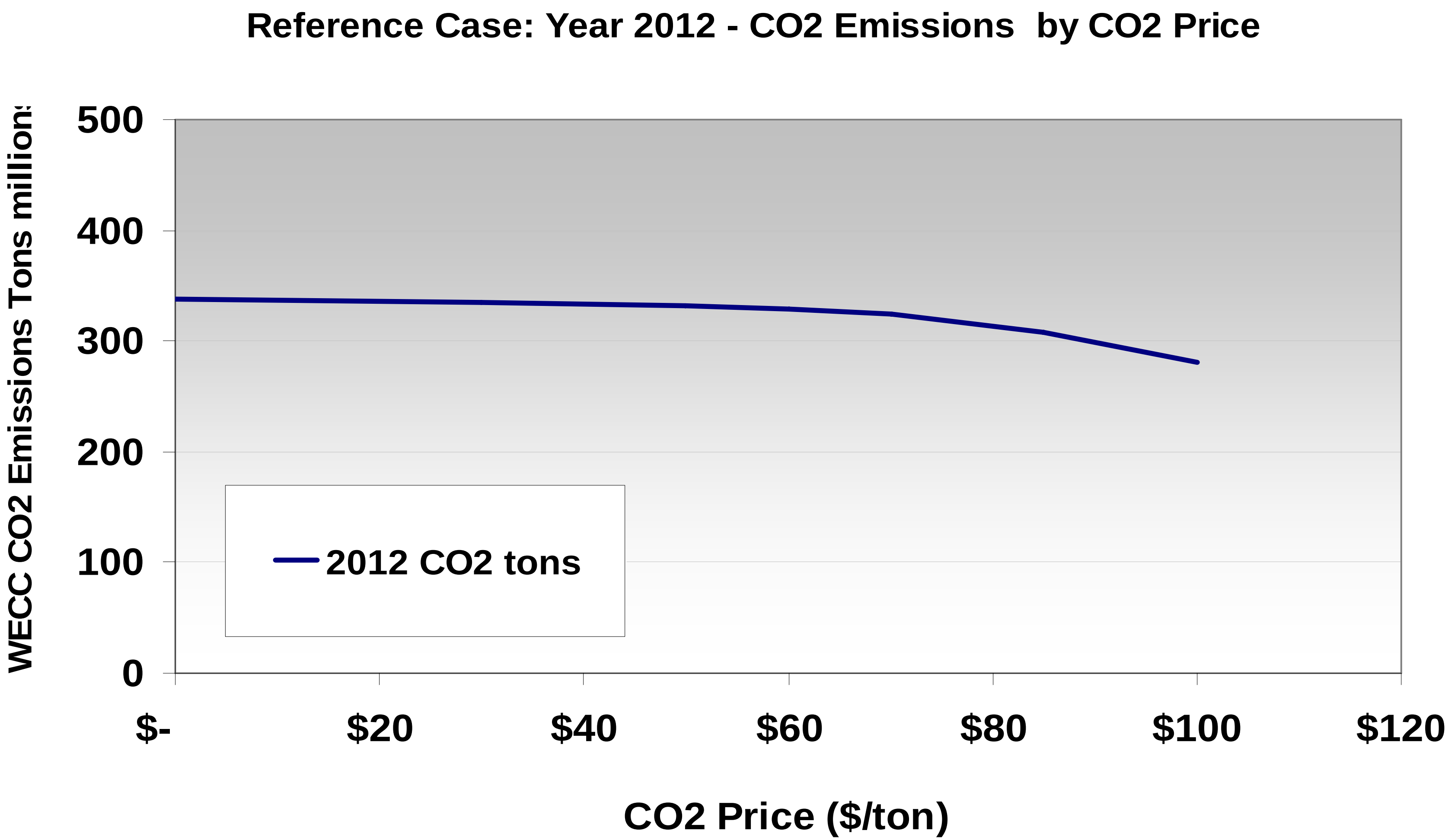


Impact of CO_2 Price on Wholesale Power Prices - 2030

Reference Case: Year 2030 - Wholesale Power Price by CO2 Price

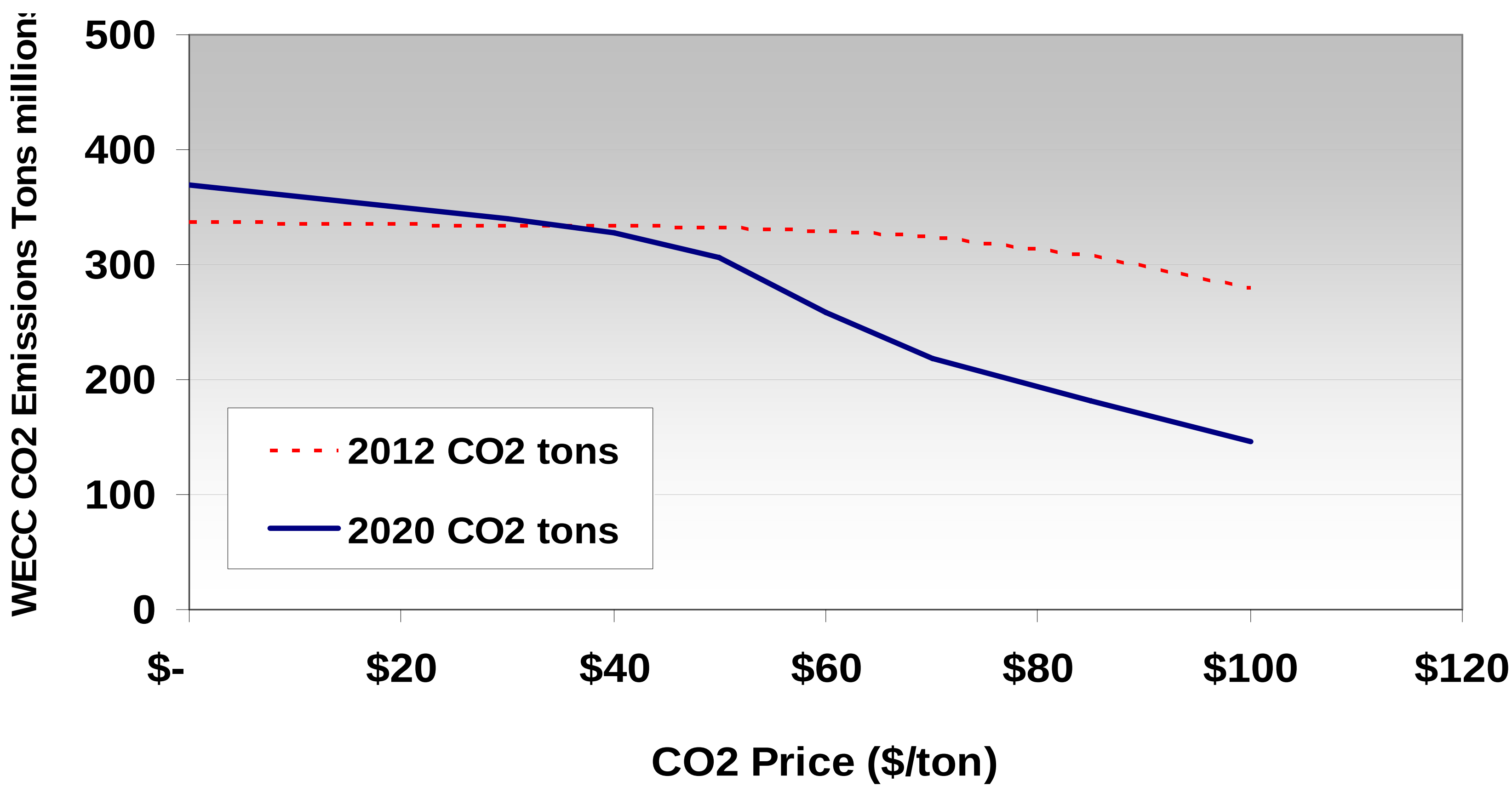


Emissions Response to CO_2 Prices - 2012

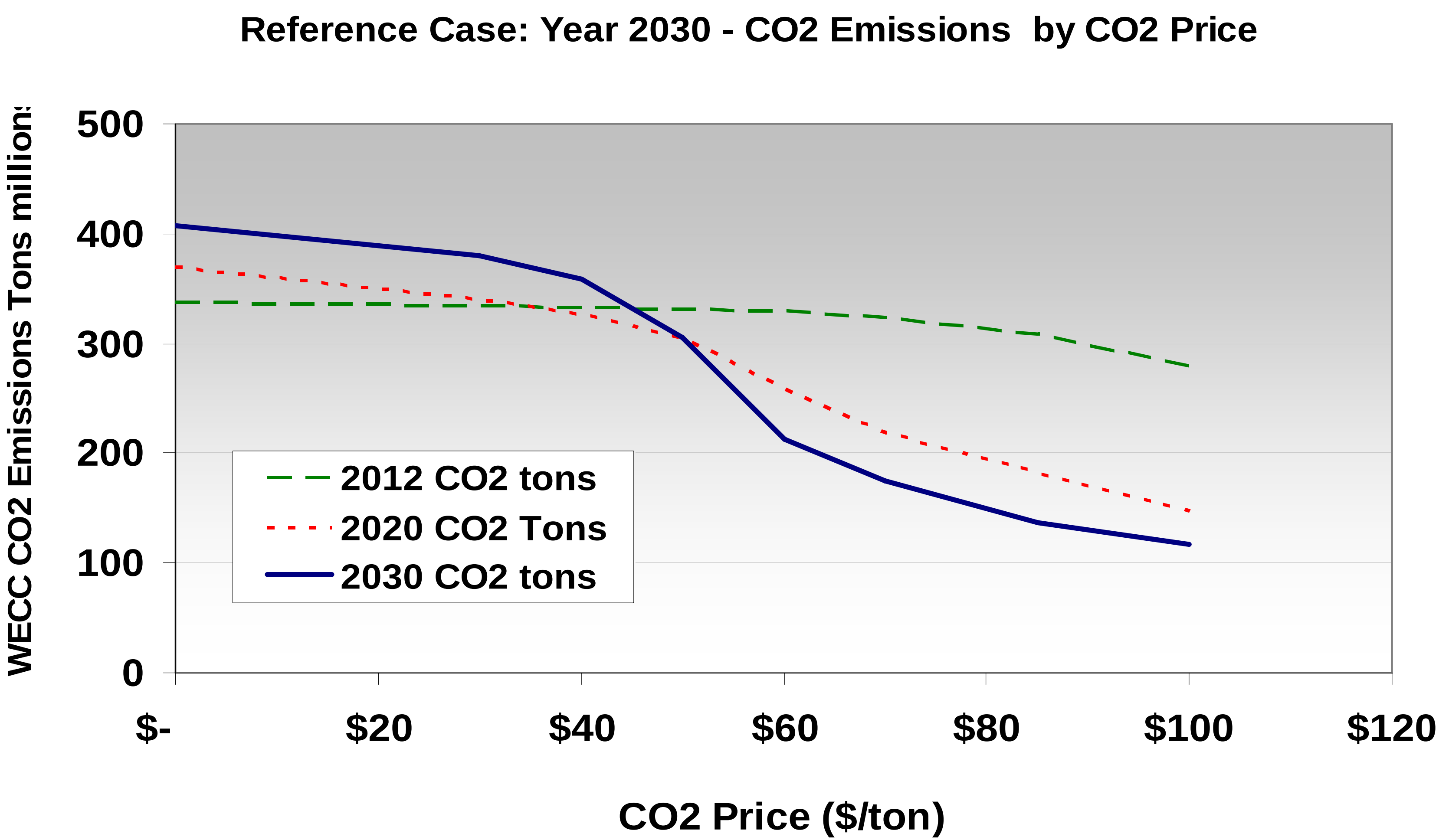


Emissions Response to CO_2 Prices - 2020

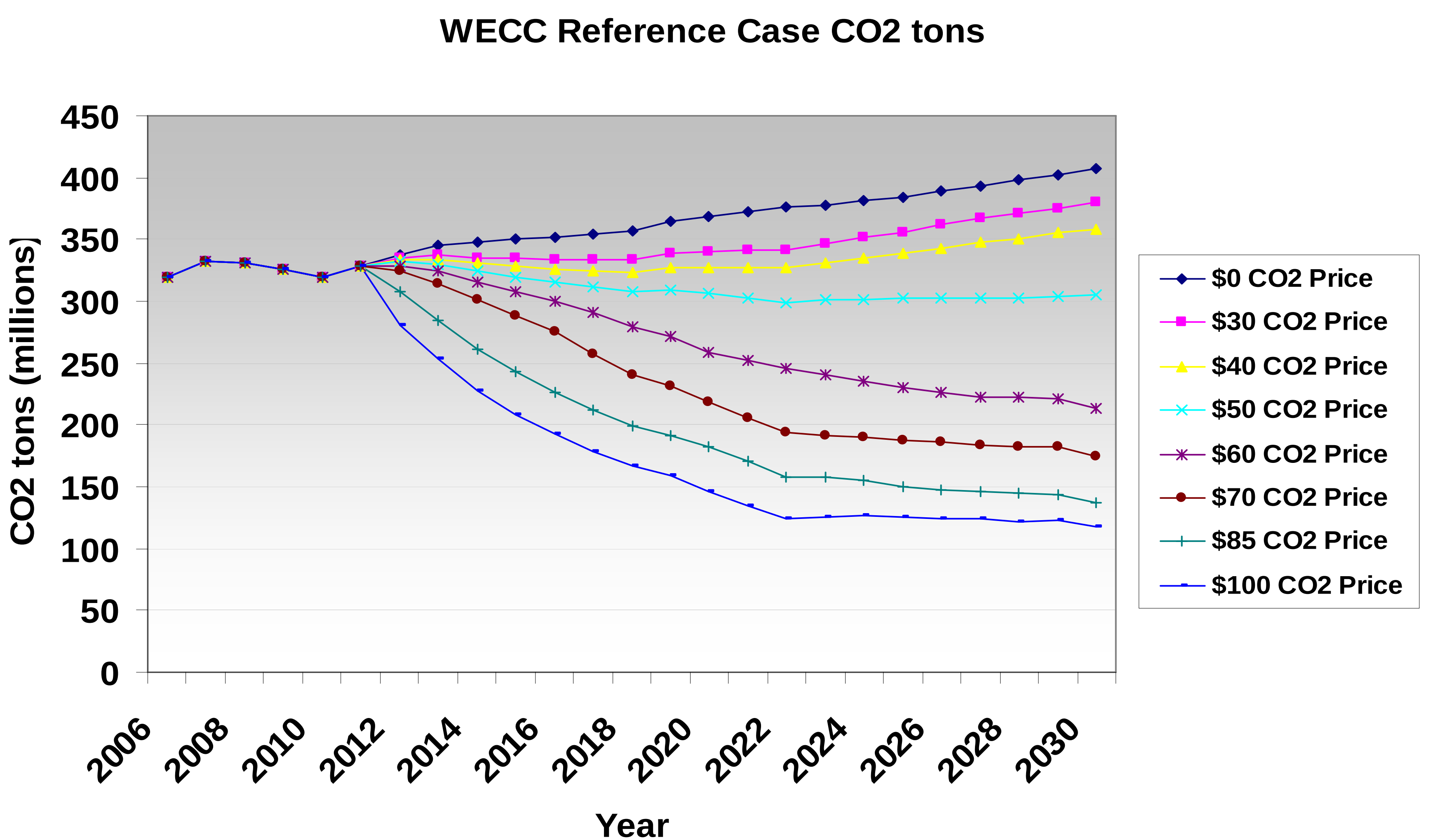
Reference Case: Year 2020 - CO2 Emissions by CO2 Price



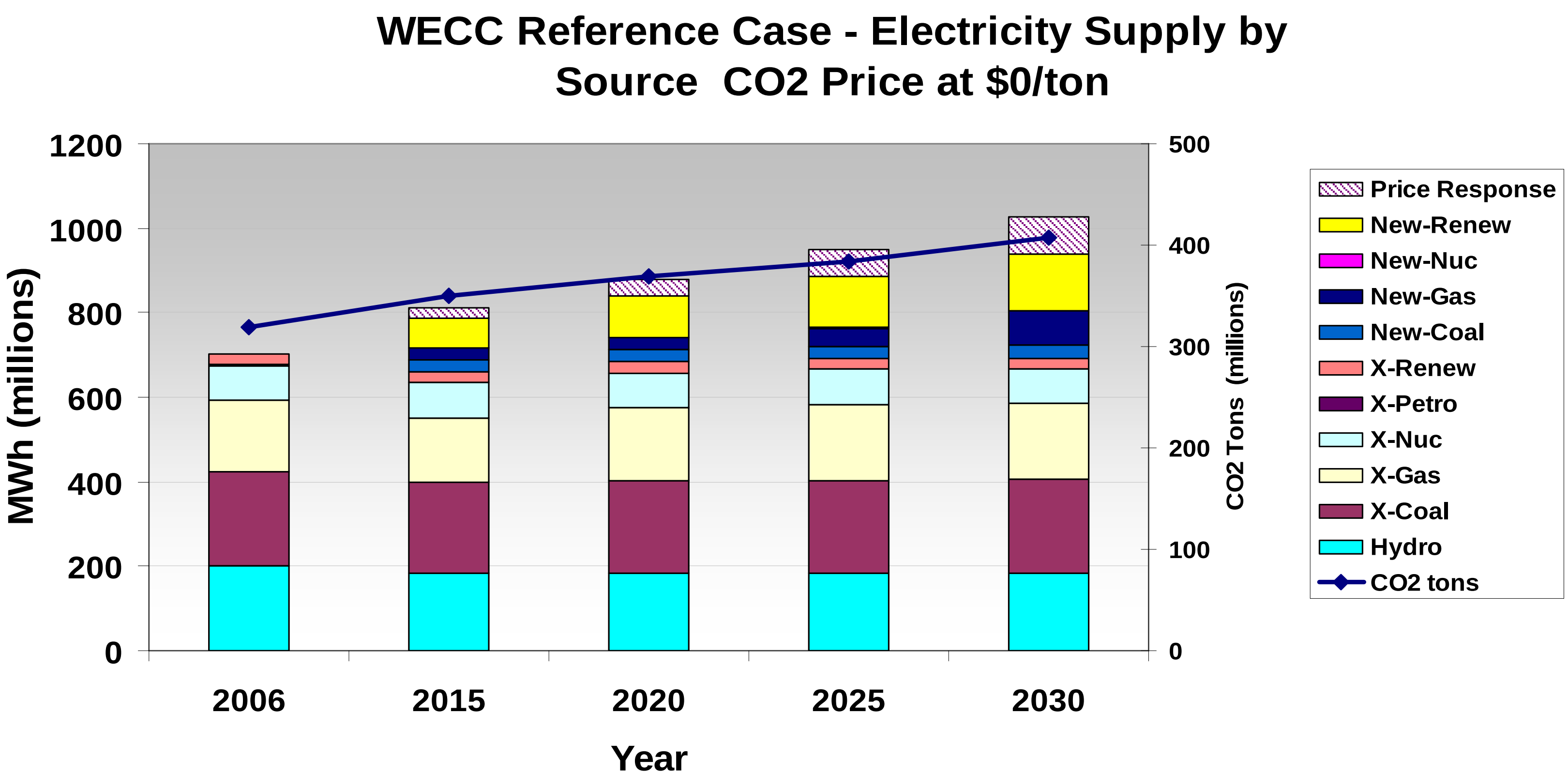
Emissions Response to CO_2 Prices - 2030



Emissions by CO_2 Price

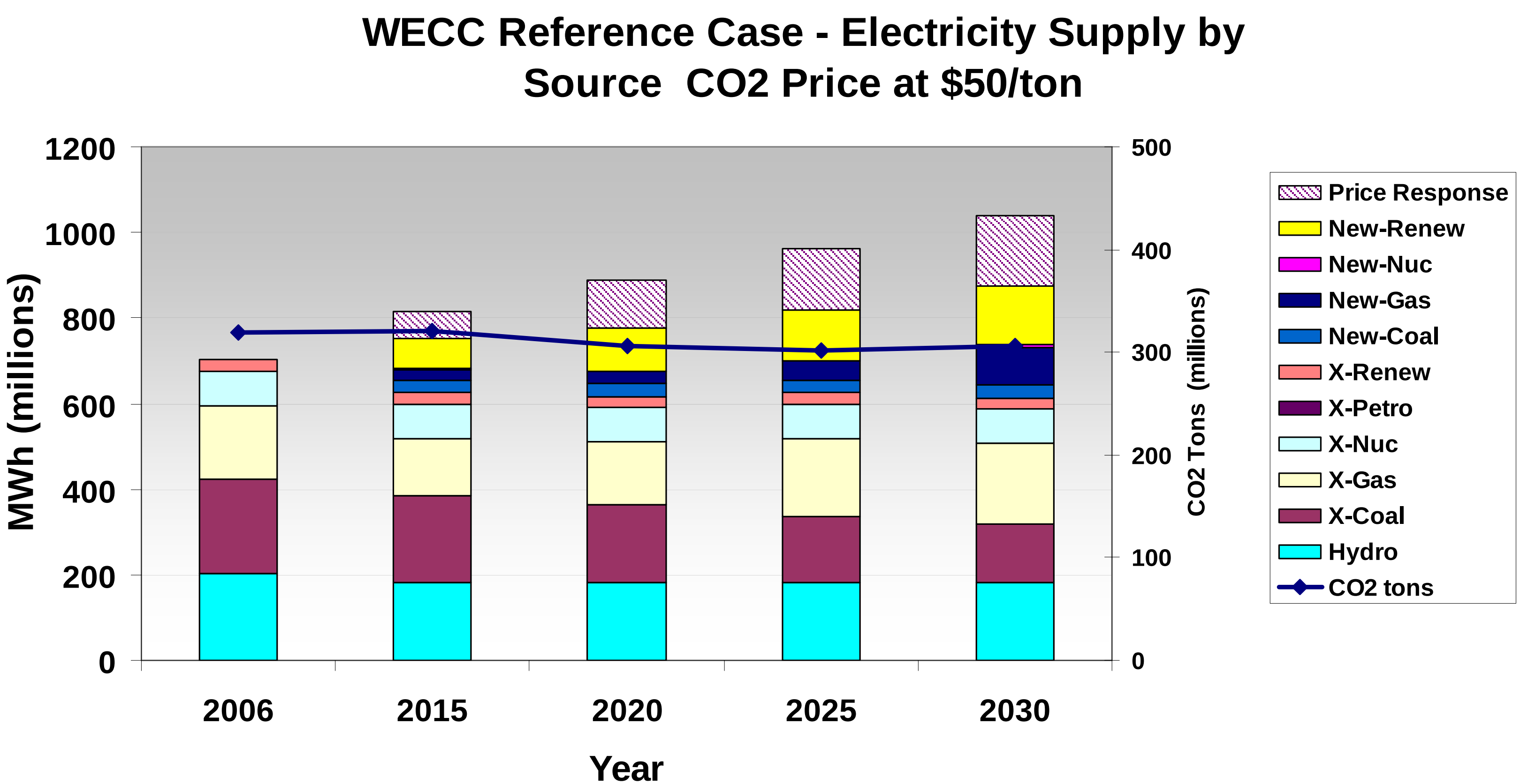


Evolution of the Generation Output and CO_2: Reference Case @ $0/ton



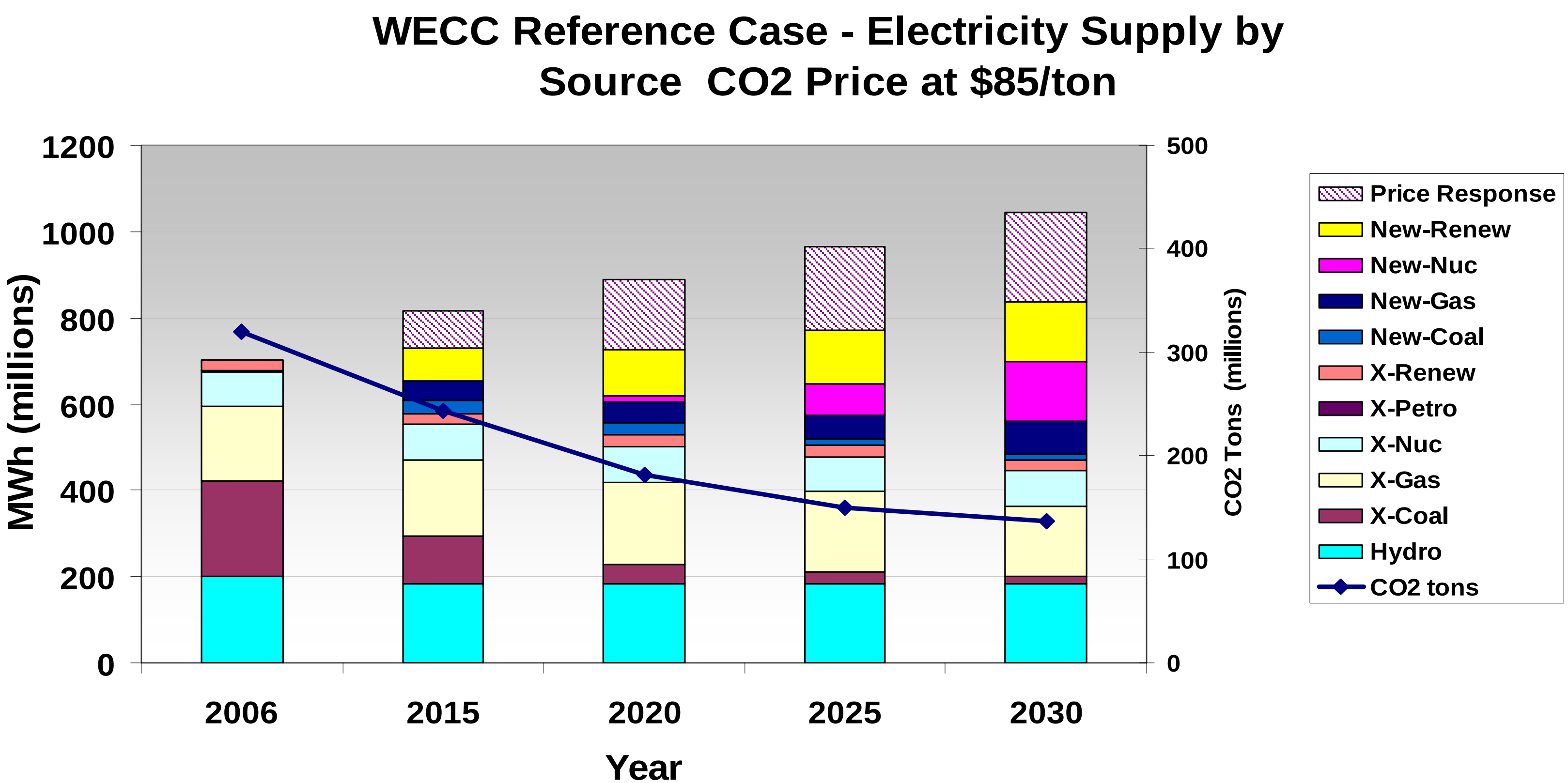
- Renewables growth keeps pace with demand; gas growth in later years
- Post-2015, existing generation is not backed out; emissions increase

Evolution of the Generation Output and CO_2: Reference Case @ $50/ton



- Coal generation declines as CO_2 price increases; gas increases
- Demand is tempered through price response
- Emissions start to stabilize once capital changeover starts

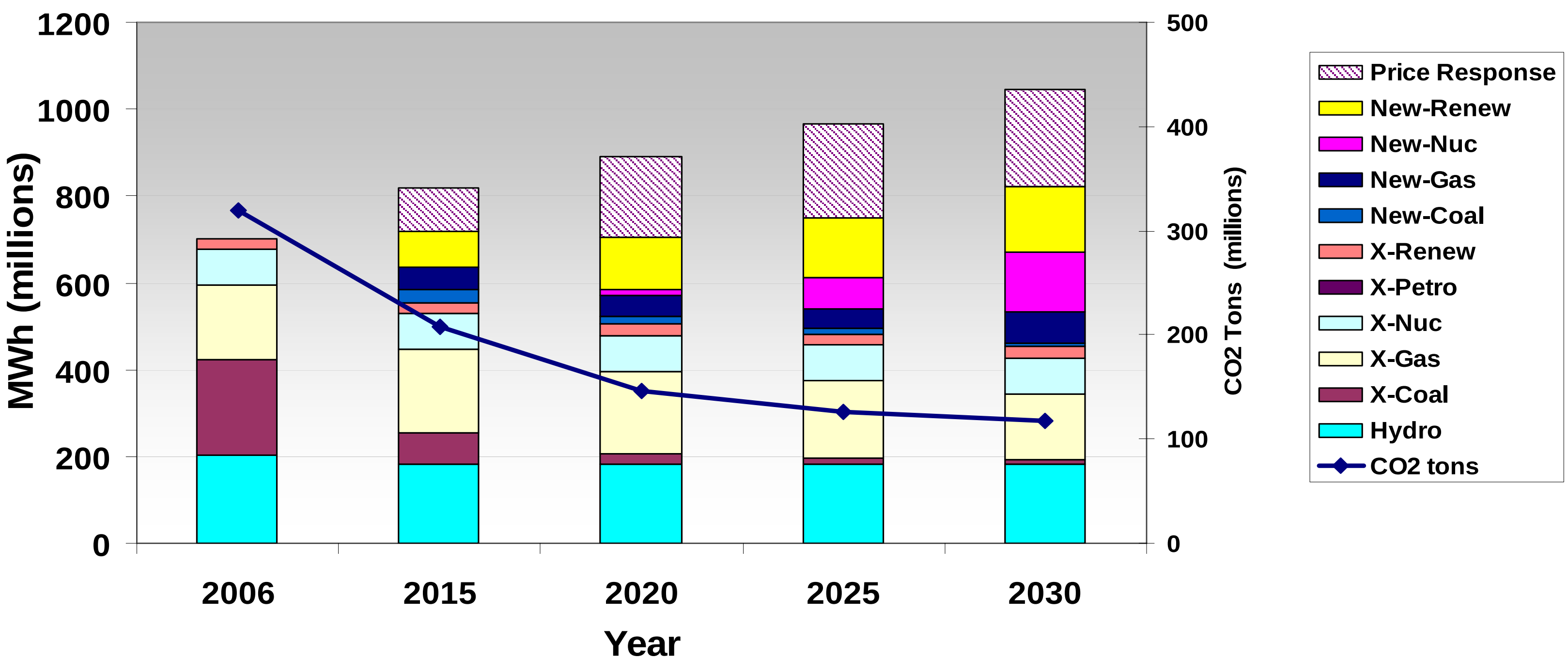
Evolution of the Generation Output and CO_2: Reference Case @ $85/ton



- X-coal generation declines further
- Non-emitting gen penetration tempers the electric price
- Price response slows down in later years
- Emissions shrinkage flattens out a bit

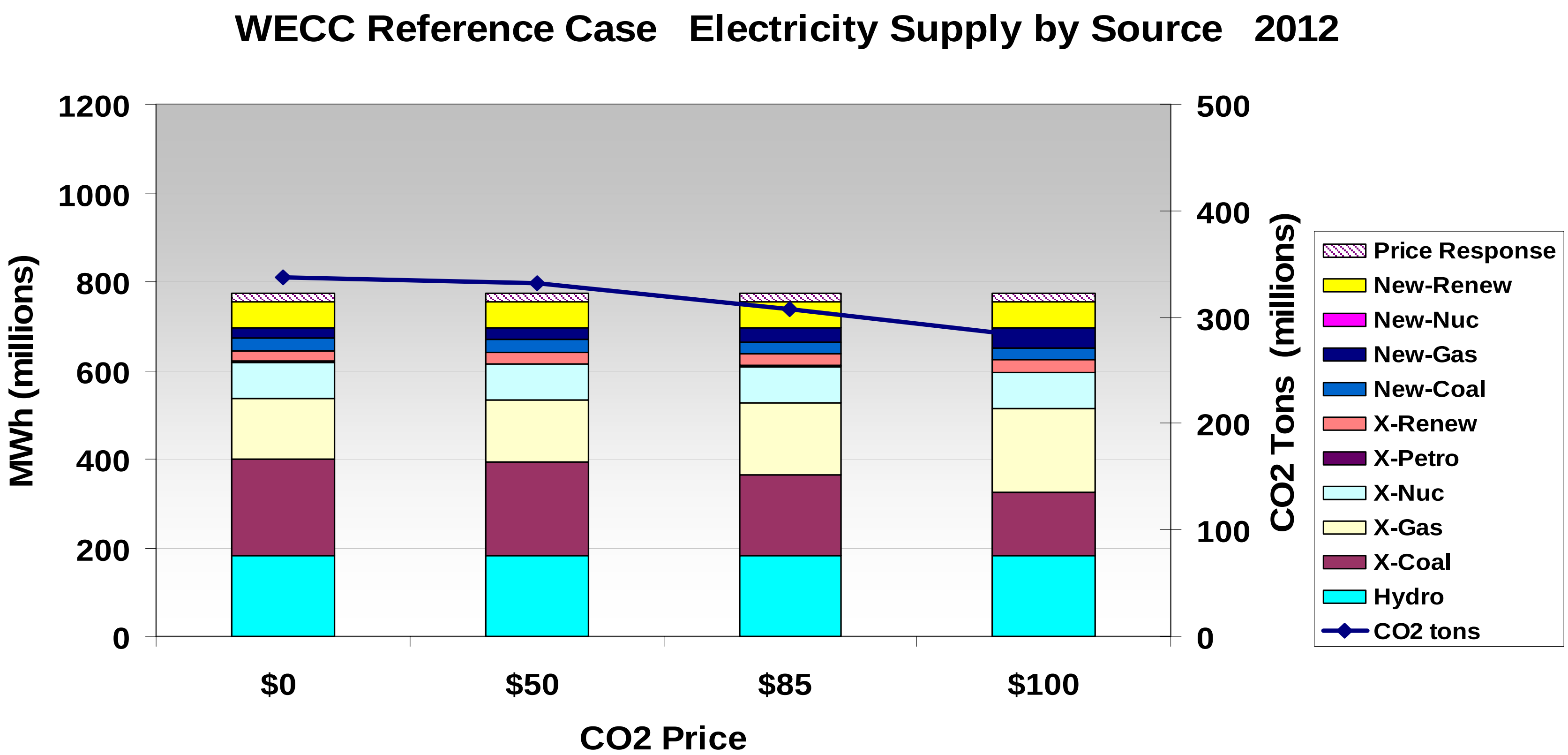
Evolution of the Generation Output and CO_2: Reference Case @ $100/ton

WECC Reference Case - Electricity Supply by Source CO2 Price at $100/ton



- X-coal generation essentially disappears at this price
- Again price response slows down in later years; emissions shrinkage flattens out a bit

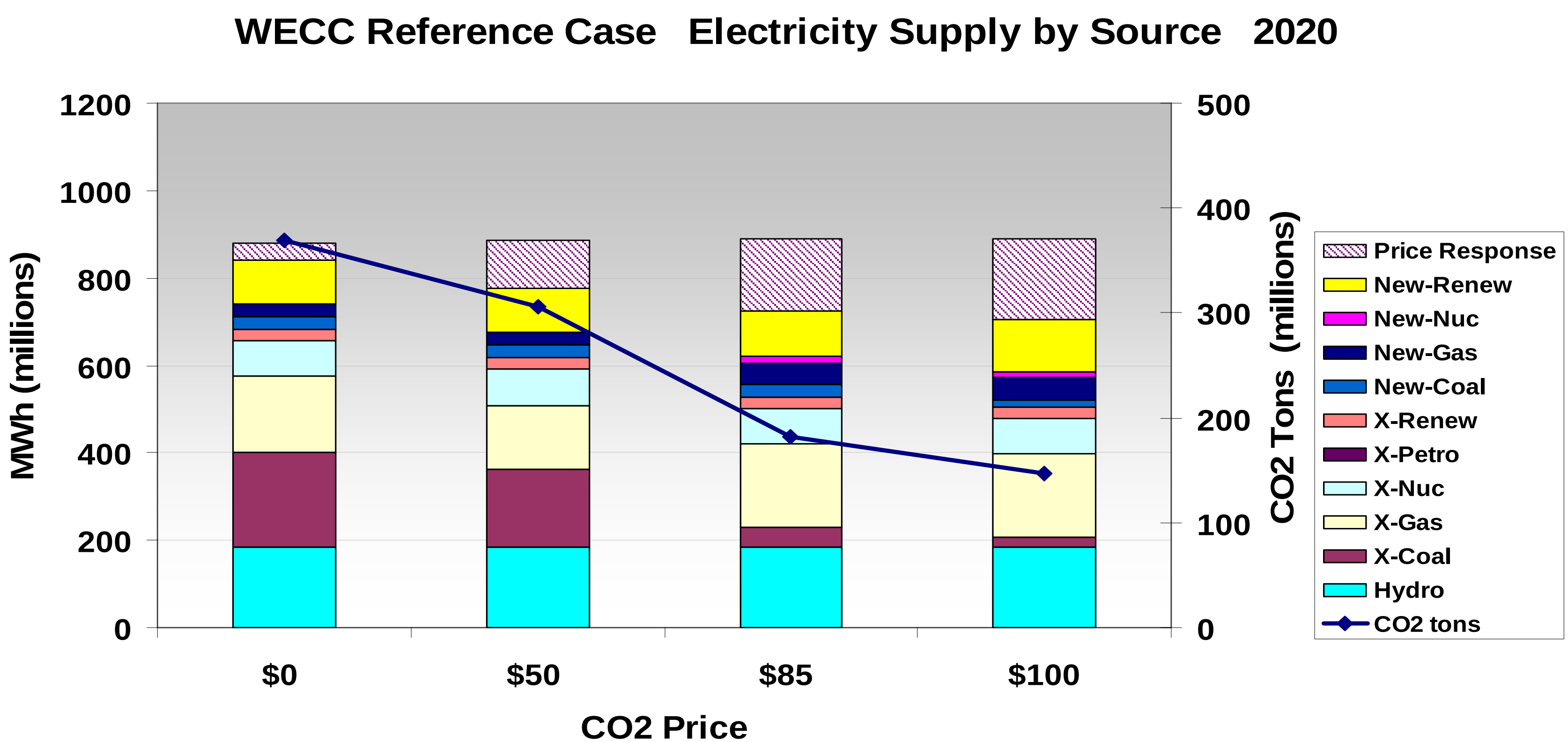
How the System Cuts Emissions: 2012



- X-gas substitutes for x-coal

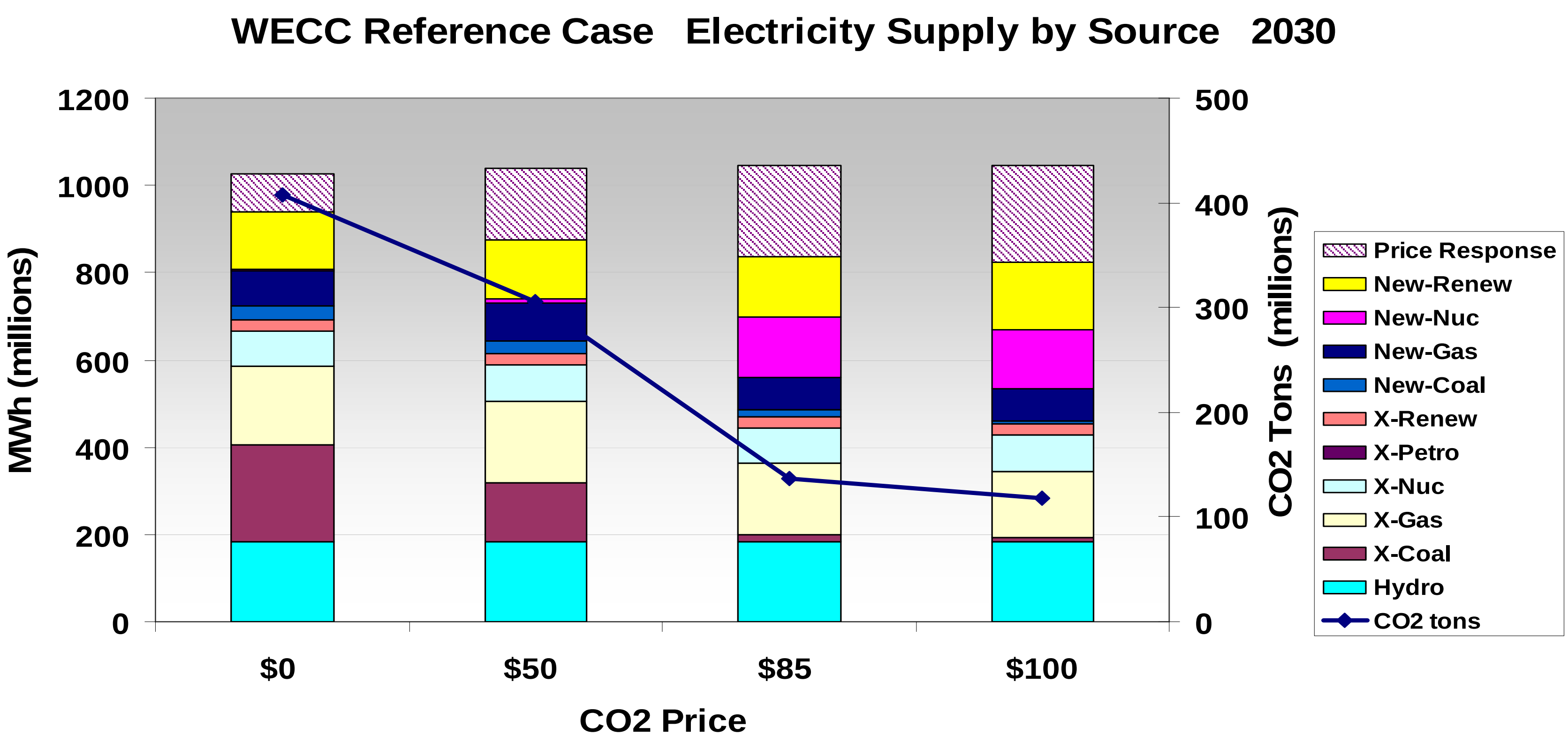
(emissions % age reduction: 1% @ $50, 9% @ $85, 17% @ $100)

How the System Cuts Emissions: 2020



- Material price increase and price response
- X-coal disappears at the higher CO_2 price levels
- Non-emitters have not yet penetrated
  (emissions % age reduction: 17% @ $50, 51% @ $85, 60% @ $100)

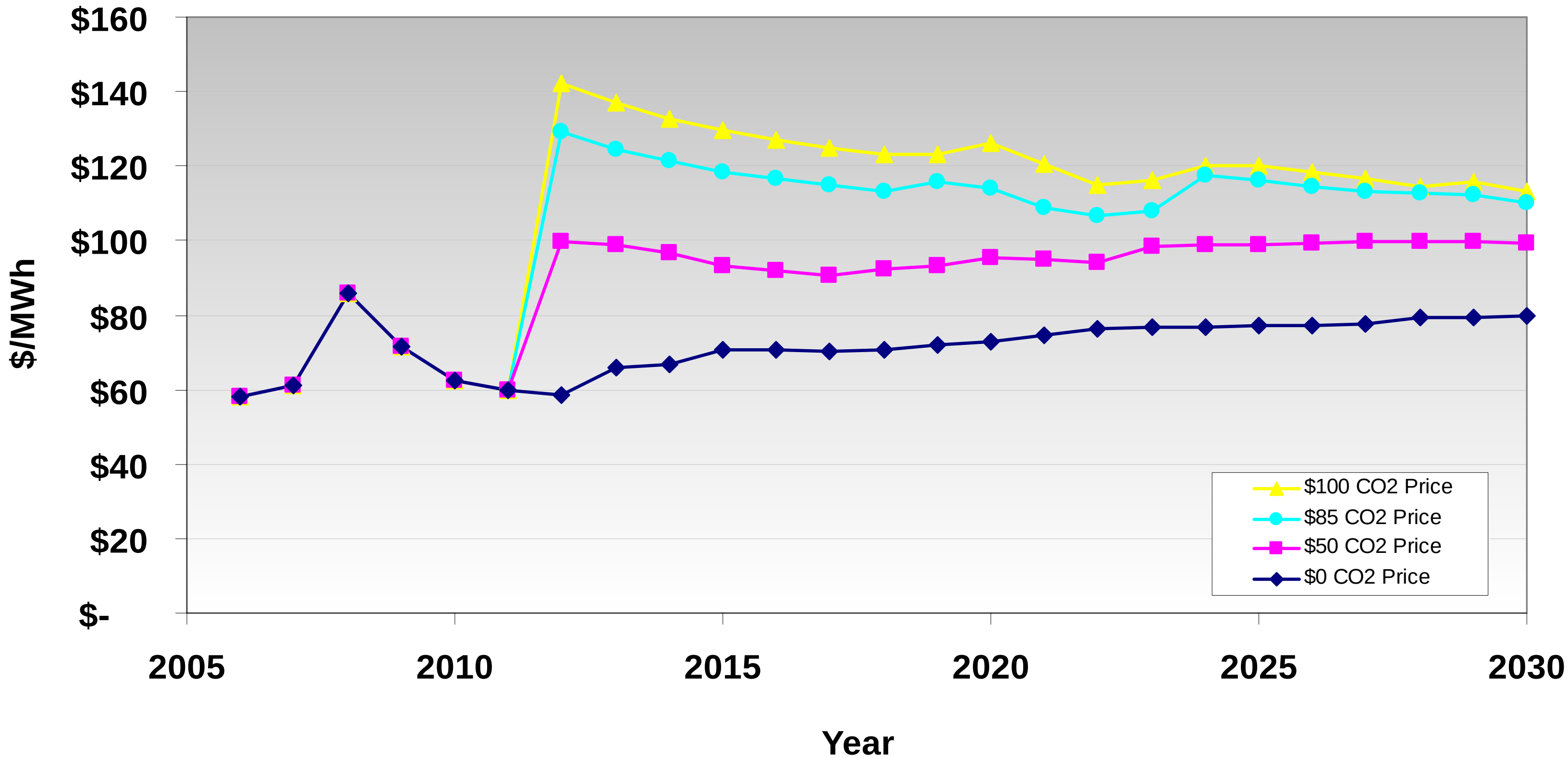
How the System Cuts Emissions: 2030



- Material price increase and price response
- Non-emitters are established in the market
  (emissions % age reduction: 25% @ $50, 66% @ $85, 71% @ $100)

Wholesale Electric Prices

Wholesale Electric Price $/MWh WECC Reference Case

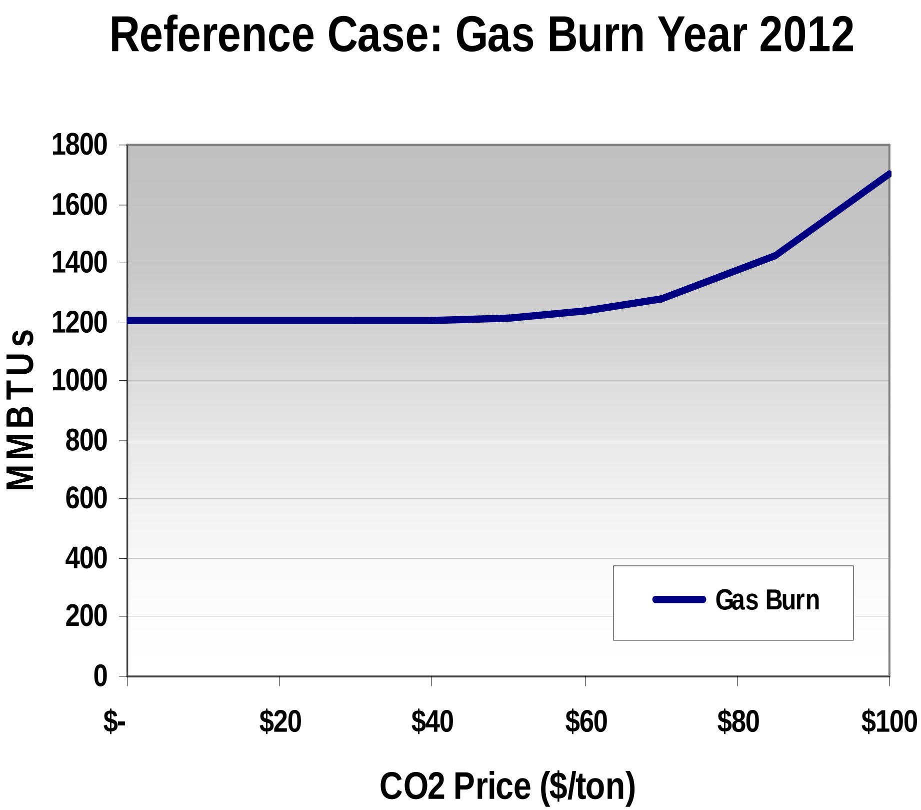


- % age increase in 2012: 69% @ $50, 119% @ $85, 141% @ $100
- % age increase in 2030: 25% @ $50, 38% @ $85, 41% @ $100

Impact of CO2 Price on Retail Electric Rates

- 2006 Benchmark
  - $94/MWh - weighted average retail price for WECC
  - $58/MWh - wholesale price for WECC
  - $36/MWh - average delivery expense (38% of retail)
- CO_2 price implications in 2012
  - CO_2 price @$0 - $95/MWh retail (1% over 2006)
  - CO_2 price @$50 - $136/MWh retail (43% increase over $0 case)
  - CO_2 price @$85 - $165/MWh retail (74% increase over $0 case)
  - CO_2 price @$100 - $178/MWh retail (87% increase over $0 case)
- CO_2 price implications in 2030
  - CO_2 price @$0 - $116/MWh retail (23% over 2006)
  - CO_2 price @$50 - $136/MWh retail (17% increase over $0 case)
  - CO_2 price @$85 - $146/MWh retail (26% increase over $0 case)
  - CO_2 price @$100 - $149/MWh retail (28% increase over $0 case)

Gas Burn Is Highly Sensitive to A Higher CO_2 Price in Early Years



- 2012 gas burn greatly increases w. high CO_2 prices

  Increased demand for gas will increase price

  Buts…
  - Electric sector 1/3 of use
  - Other 2/3 will have incentive to cut demand ($1/ton → $0.058/MMBtu)
  - LNG may be swing supply
- **Impact on gas market a critical unknown**

Summary of Sensitivity Analyses

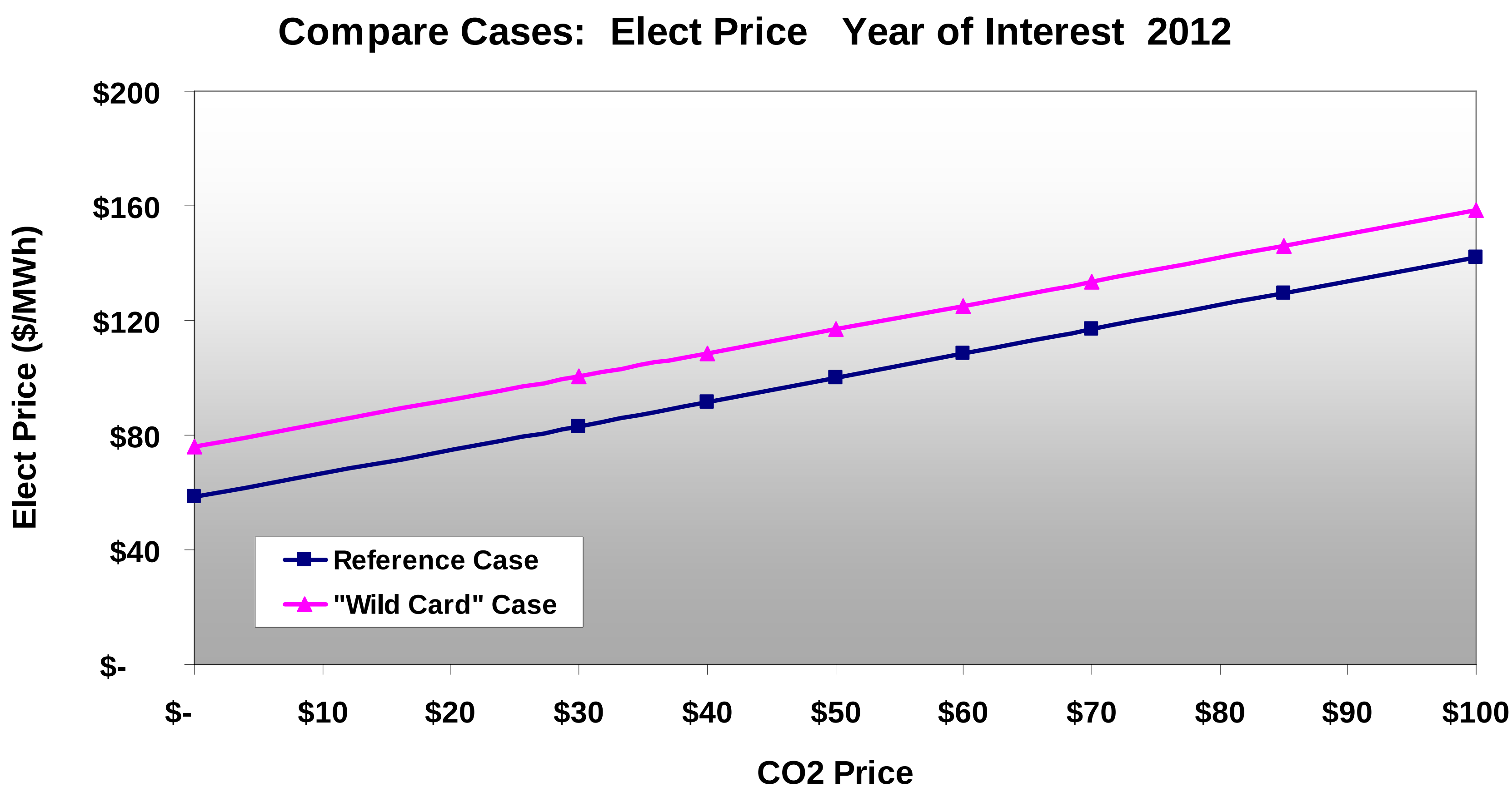
- Gas prices higher than projected
  - Higher emissions absent a price, but higher CO_2 price reverses this
- A high load growth case driven by PHEV penetration
  - Higher power emissions, more than offset by transportation reductions
- Higher capital costs for new generation
  - Delayed emitter to non-emitter turnover; higher prices, higher emissions
- No new nuclear generation is built in future
  - Renewable technologies and new gas substitute, but power prices/emissions higher
- "Wild Card" - several adverse outcomes happen simultaneously
  - With multiple drivers negatively impacted, response flexibility is limited
  - Much higher power prices and emissions
- R&D success for CCS
  - Provides a valuable alternative to nuclear, renewables
  - Major source of generation supply if nuclear is limited

The "Wild Card" Case:
Defined by a Collection of Adverse Outcomes Simultaneously

- High load growth
  - 2.2% annually
- High gas prices
  - $2 above Reference Case
- Low customer demand response
  - (0.25) long term price elasticity
- High plant capital costs
  - 25% above Reference Case
- No new nuclear
  - constrained from capacity addition pre-2030

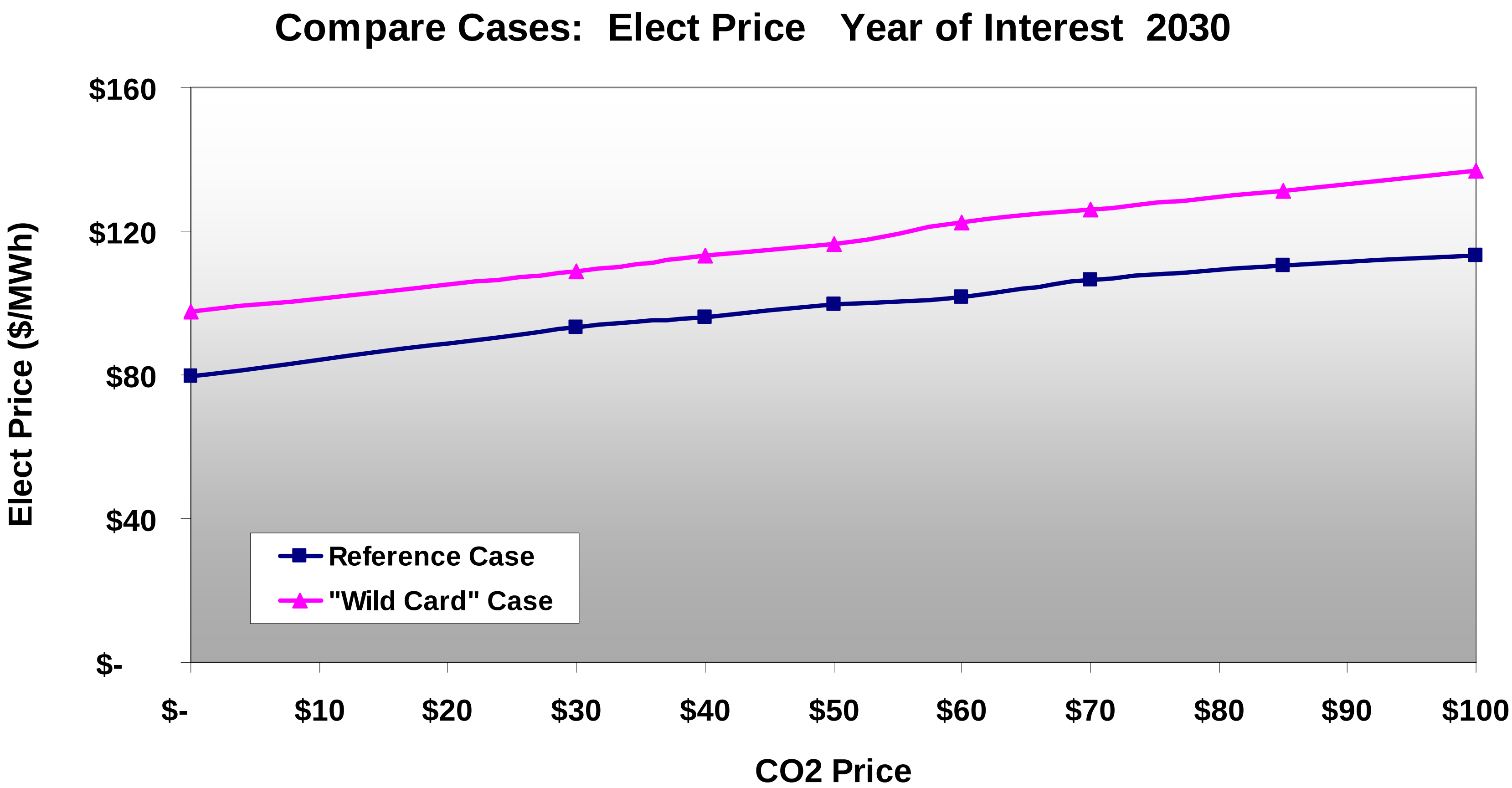
The "Wild Card" Adverse Outcomes Case: 2012

Electric Price



- Electric prices rise for the most part proportionately
- Tempered slightly at higher CO_2 prices by the increase in coal burn

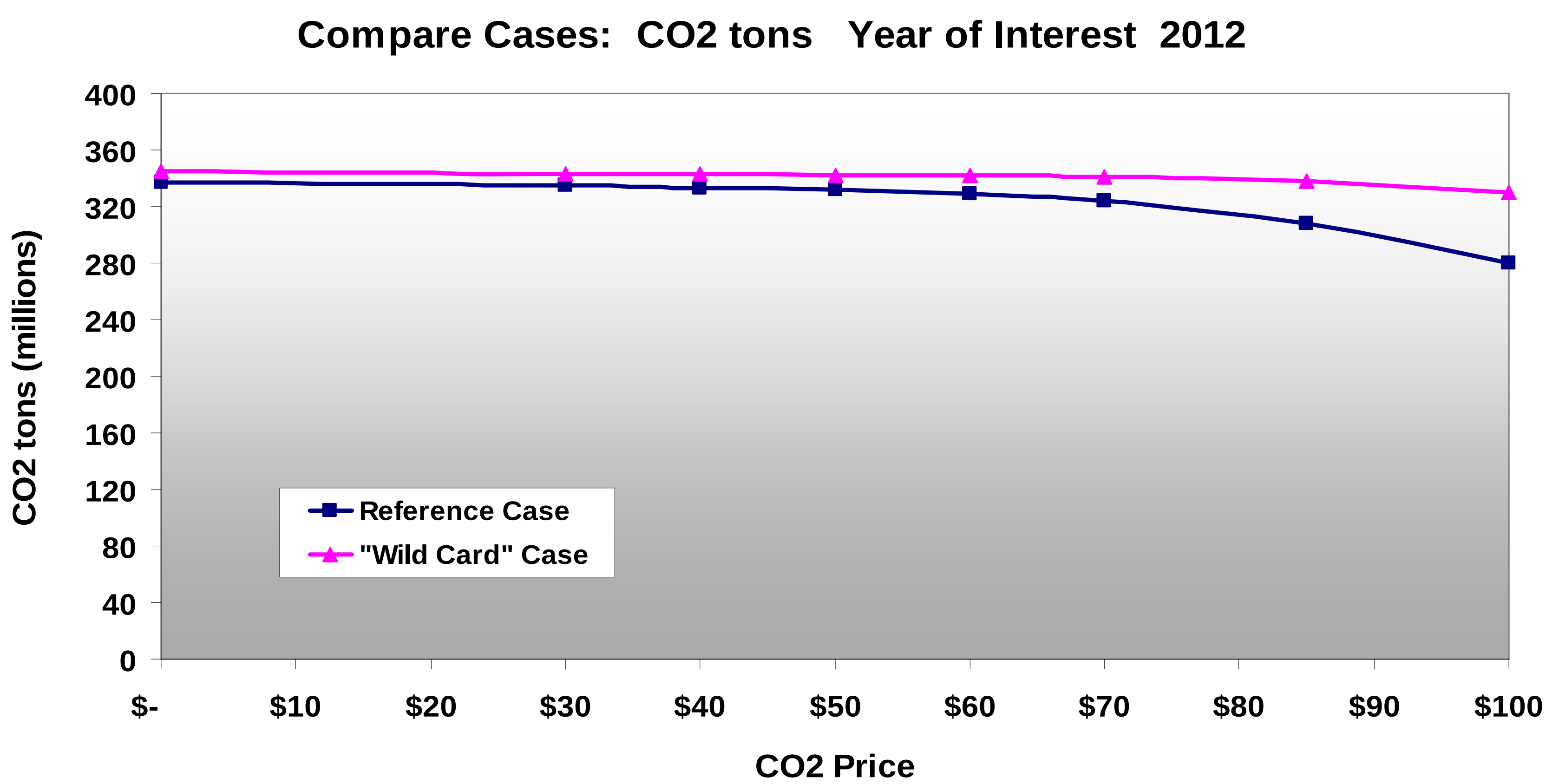
The “Wild Card” Adverse Outcomes Case: 2030
Electric Price



- Electric prices must be high enough to encourage new resources at higher plant costs for the “Wild Card” case

The “Wild Card” Adverse Outcomes Case: 2012

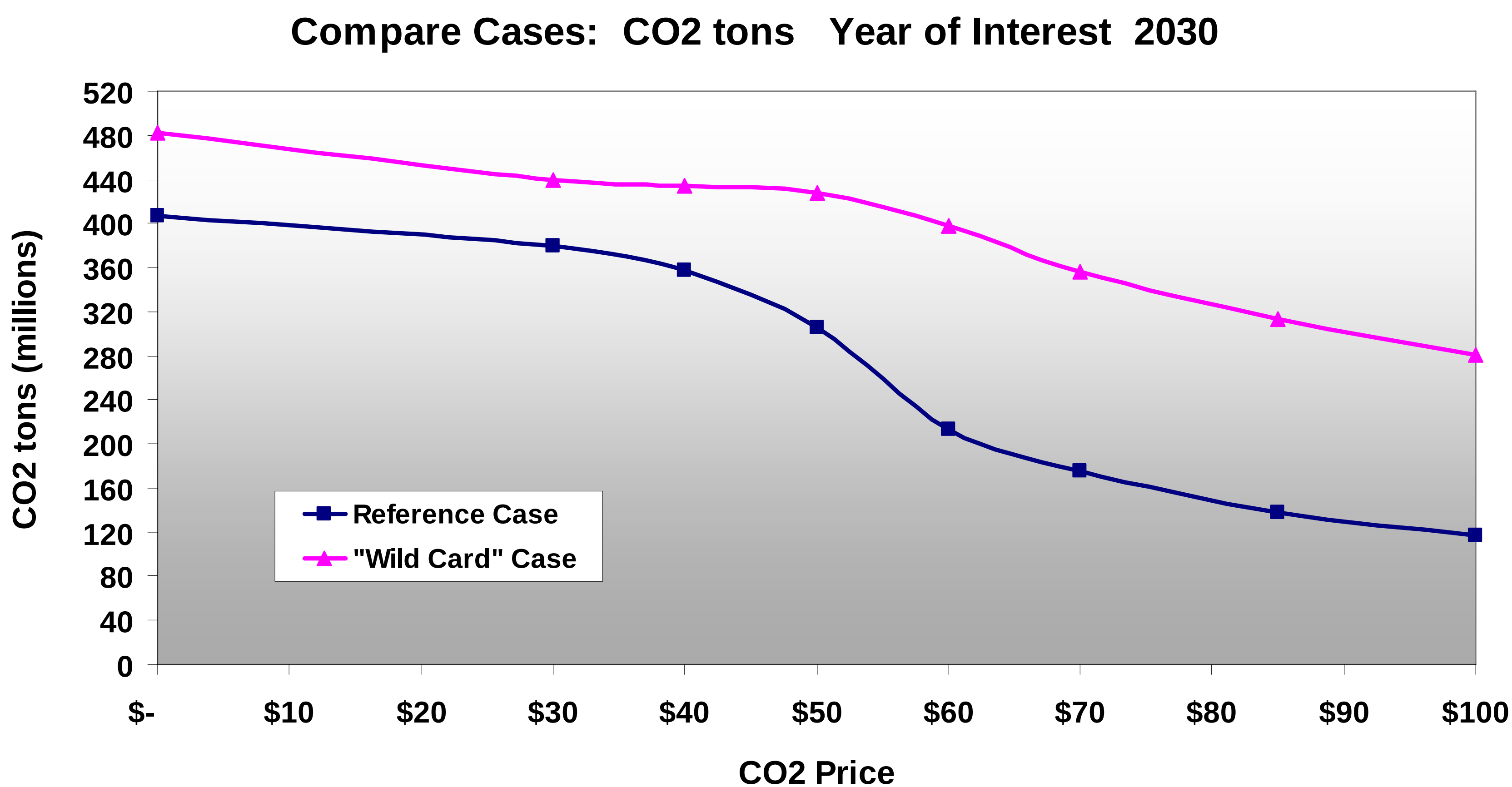
Emissions



- “Wild Card” case has only modest emissions impact in 2012
- Higher gas prices force higher coal burn
- Gas price differences become more acute at higher CO2 prices

The “Wild Card” Adverse Outcomes Case: 2030

Emissions



- Higher cost of new plant, nuclear constraint, leads to more generation from existing coal, higher emissions

Conclusions

- Higher electric prices will be inescapable in order to cut CO_2 emissions below historic benchmarks
  - $50 CO_2 price stabilizes emissions (retail price +45% in 2012, +15% in 2030)
  - $75-$100 CO_2 price significantly cuts emissions (retail price +90% in 2012, +30% in 2030)
- In a "Wild Card"/adverse effects world…
  - $75 min price achieves stabilization (retail price +60% in 2012, +20% in 2030)
  - $125-150 price achieves significant cuts (retail price +100% in 2012, +37% in 2030)
- Large reductions in emissions possible if given time to add significant amounts of nuclear, renewables and CCS
- Customer price response helps avoid emissions but imposes real cost to society
- Availability of natural gas critical to achieving near term emission reductions
- RPS threshold adding gen that cuts CO2 at implied price of $90/ton

What I learn from this

- It's expensive to cut electric sector emissions due to…
  - High price of natural gas (vis-à-vis coal)
  - High cost of new construction
- Lot's of uncertainties drive specific results
  - Gas prices, construction costs, constraints on nuclear and renewables, demand response, new technology
  - Response of gas market to increased gas generation
- Meeting targets may be harder in the short term due to lead-times for new generation and demand response

Final Thoughts

- This analysis should be viewed as a interim step in an ongoing study of a critical but complex issue
- Feedback and comments from all parties are appreciated
- Next steps
  - Post slides at **globalclimate.epri.com**
  - Next presentation week of June 23rd (contact Vic or Lew for notice)

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