Always on

Reliable electricity in an age of coal plant retirement
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Traditional baseload power plants are increasingly obsolete. The 21st-century electricity system is much more diverse and dynamic. Electricity is now managed through very large, regional energy markets. Today’s regional power grids serve millions of individual loads by combining electricity from many power plants—of which, at any given moment, some are operating and others are not. In the past, baseload power plants emerged as the best way to ensure a reliable, low-cost supply of electricity in smaller, localized systems. Today, shifting market forces and technological innovations are changing the equation. As states across the country evaluate how best to provide affordable, reliable, and sustainable electricity services, this changing paradigm will be at the center of their planning considerations.

WHAT IS BASELOAD POWER AND WHY WAS IT SO IMPORTANT?

The electricity system that was built from 1970 to 2000 relied on what have become known as baseload power plants—very large, centralized plants designed to operate nearly all the time. The most common examples of baseload generators are coal, nuclear, and large hydroelectric power plants. These facilities are very hard to ramp up and ramp down—coal and nuclear in particular can take days or even weeks to become fully operational. Because of this inflexibility, baseload power plants are designed to meet the core amount of demand required by utility customers and are rarely shut off. Other, more agile generation sources, such as those powered by natural gas, are quickly brought online when demand increases and are subsequently taken offline when demand returns to its minimum baseload level, usually in the middle of the night.

In the past, baseload power plant resources were used because they cost less to operate and were more reliable compared with alternatives. They were also perceived as low-risk investments because demand for electricity was growing at a rapid and consistent pace. Like all utility investments, baseload power plants are paid for over time through rates charged to consumers. Even though traditional baseload power plant projects required enormous amounts of capital to construct, consistent demand growth meant that the costs of a new plant could be recouped from ratepayers over many years and without large rate shocks. This trend broke down during the recessions of the 1970s and 1980s, when ratepayers lost billions of dollars because they were charged for planned baseload power plants that were abandoned before or after construction or underutilized for years.

MARKET CHANGES HAVE REDUCED THE VALUE OF TRADITIONAL BASELOAD POWER PLANTS

Over time, market changes in the electricity sector have eroded baseload power plants’ low costs and improved the costs and reliability of competing generation sources.

- Construction costs of large power plants continue to increase due, at least in part, to the rise in global demand for building materials. Additionally, large power plant construction has already incorporated available economies of scale—costs are as low as they are likely to go. In contrast, the cost of solar and wind manufacturing continues to fall because the equipment is small in size and modular, and construction costs benefit from increasing economies of scale. Baseload power from new coal and nuclear generating facilities is increasingly more expensive than alternatives.

- Fuel costs for traditional baseload power plants are also rising due to global demand. From 2000 to 2010, the price of coal delivered to utilities nearly doubled, despite the economic slowdown.

- Government agencies are increasingly holding electricity generators responsible for associated adverse health and environmental impacts. New standards are requiring traditional baseload generators—especially coal-fired power plants—to internalize costs that were previously transferred to citizens’ health and environmental clean-up costs.

- Demand growth for electricity has dropped dramatically over the last few decades and is expected to grow much more slowly in the future. A combination of energy efficiency improvements in existing buildings and more stringent appliance standards are the expected drivers in slower demand growth. Ratepayers are exposed to large amounts of risk if a company builds a new, large baseload power plant when the company’s demand is not growing fast enough to guarantee that small rate increases will pay for the plant over time.
INNOVATIONS ARE CREATING A NEW, MORE FLEXIBLE, AND DYNAMIC SYSTEM

The existing electricity system was built around baseload power plants while utilizing other, more flexible power sources to meet periods of higher demand.

Now, for reasons that include the market effects just mentioned, states and utilities are choosing to add significant amounts of renewable resources to their energy systems. Minnesota has a Renewable Electricity Standard that was developed to help the state achieve its goal of obtaining 25 percent of its electricity from renewable sources by 2025, and many other states have similar goals. These renewable energy additions are changing the composition and operation of the regional electricity grid. The managers of the regional electricity grid have developed and are continuing to develop ways to increase reliability and complement the variability inherent in wind and solar resources. These innovations are creating a flexible and dynamic system to deliver reliable and cost-effective electricity in the 21st century. As renewable resources are paired with other, more flexible generation sources within much larger regional systems, traditional baseload power plants no longer serve the critical role they once did.

Innovations that are reducing cost and variability:

- Wind reached cost parity with traditional energy sources several years ago, and solar costs have been dropping by at least 7 percent annually for the past 10 years and are expected to continue on that downward trend.

- Grid operators and utilities are using more agile resources, like natural gas plants, to complement the variability inherent in renewable generation. Natural gas plants were used in the old system to quickly ramp up and down with changes in customers’ electricity demand. In the new system, they can be deployed to ramp up and down with changes in demand and supply. There is presently a glut of capacity in existing natural gas plants that can be cost-effectively and quickly deployed, especially if gas prices remain low for the long term.

- Grid operators are improving their ability to follow customer demand more closely. New innovations in demand response and load management allow utilities and grid operators to increasingly rely on the ability to quickly reduce customer demand when needed through voluntary agreements with commercial and industrial users.

- Improved planning tools are enabling grid operators to more accurately predict when changes in renewable output will occur and to plan complementary resources accordingly.

- Regional electricity grids are becoming more connected and able to transmit and optimize power across longer distances. As the geographical footprint of the electricity grid expands, the amount of solar and wind resources available at any given time also increases. The more geographical diversity in a grid operator’s area of control, the more the operator can optimize variable generation resources to meet demand.

CONCLUSION

In today’s energy system, traditional baseload power plants’ strengths have become less relevant and weaknesses more pronounced. Market forces are eroding baseload power’s cost advantages and increasing its cost risks. At the same time, competing sources of power generation are becoming cost-competitive while technological and process innovations are enabling utilities and grid operators to maintain and improve system reliability. As policymakers and regulators strive to provide affordable, reliable, and environmentally acceptable electricity, traditional baseload power plants will continue to have less value in the 21st-century electricity system.
Once in operation, traditional baseload power plants produce power at a relatively set rate and efficiency level. Regional grid operators are able to utilize modern technology and forecasting tools to provide consistent and quality electricity.

Most of the nation’s traditional baseload power plants were constructed in the second half of the 20th century. Aging infrastructure, upgrades, and pollution control equipment add substantial operating costs. Many smaller, modern generation facilities are newly constructed and require little cost to operate. Maintenance is minimal and new technologies and pollution mitigation equipment often already exists.

Because of their large size, traditional generating plants are very costly to construct. Financing of such large facilities can be difficult and costly to secure and can be seen as a risky investment. Smaller, modern generation facilities are more modular and can be built to fit the need, reducing the upfront costs. As this system becomes more and more prevalent, economies of scale will continue to bring down the price.

Traditional baseload plants are meant to run constantly at a designated generation level and can take days or weeks to ramp up or ramp down as demand for electricity changes. More agile generation sources are quickly brought online when demand increases. Using modern forecasting and a technologically integrated system, we can more accurately match supply with demand, reducing excess generation costs.

Traditional generation relies heavily on finite resource fuels. As global competition for these resources intensifies and the world-wide supply decreases, fuel to power traditional generation plants becomes increasingly financially risky. The modern electricity system relies more heavily on cleaner fuel sources. Once up-front construction costs are paid off, many of these fuels, such as wind and solar, carry little or no fuel cost and are not subject to market volatility.

Traditional generation facilities rely heavily on fossil fuels and uranium to generate electricity. Utilization of these fuels sources comes with undesirable health impacts, including exposure to mercury, air pollution, and radioactive waste. Cleaner, modern generation does not rely as heavily on fossil fuels, and thus comes with fewer public health impacts due to generation.

Generation using fossil fuels also emits mercury and sulfur dioxide and creates air haze. Mining of traditional fossil fuels leads to habitat degradation and possible environmental contamination. Cleaner, modern generation does not rely as heavily on fossil fuels. While these create less environmental damage overall, extracting natural gas (especially through hydraulic fracturing) has a range of impacts which must be addressed.

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Minnesota’s electricity system will undergo tremendous changes in the years ahead. Many critical components of the electricity system are transforming, forcing system planners to think differently about how to provide electricity service to the state. These changing factors include:

- The natural turnover of an aging fleet of power plants
- Shifting fuel costs and availability
- Increasing availability of clean electricity technologies
- Increasingly regional system operation that integrates diverse technologies seamlessly
- The economic development potential for Minnesota to make more electricity from its own resources
- The opportunity to diversify electricity generation sources to provide greater stability and reliability of the system
- New or expected environmental standards to reduce the dangers aging power plants pose to our air, water, health, and climate

The electricity system that was built in the 20th century relied on what have become known as baseload power plants—very large, centralized plants designed to operate nearly all the time. Usually coal, nuclear, or large hydropower plants, these baseload plants were chosen by utilities and regulators as the optimal way to provide electricity service. These power plants were not perfect, as discussed in this report, but they became the anchors of the electricity grid.

In the 21st century, the electricity system is becoming much more diverse and dynamic. As a result of this evolution, the individual baseload plant is becoming increasingly obsolete. Electricity is now managed through regulated regional energy markets that cover broad geographic regions of the country. Today’s power grid serves millions of individual loads by combining electricity from many power plants—of which, at any given moment, some are operating and others aren’t. New technologies and forecasting methods are enabling planners to create new ways of providing reliable, affordable electricity without the drawbacks of the traditional baseload power plant technologies. The felt need to meet baseload demand with a power source that is “always on” is raised as a premise to retain these large, centralized power sources. However, these same energy demands can be met easily by our integrated and nimble grid and its diverse energy generation. Minnesota policymakers will face questions about the need for baseload power plants again and again in the years ahead—particularly given the large number of coal plants facing retirement—making it important to understand what baseload power is and what it is not.

PROVIDING POWER: WHAT WE NEED

Electricity is a commodity, but one with special characteristics that pose unique challenges. Demand for electricity is immediate; it must be available at the flip of a switch. Demand is variable, always changing as we turn on our appliances or turn off heavy manufacturing machinery. Supply is also variable—a power plant’s output is never entirely uniform, requiring regional grid operators to constantly manage generation resources across multiple states. Until utility-scale electricity storage becomes an economic reality, grid operators have to instantaneously match generation supply with consumer demand.

There are three metrics that planners keep in mind when balancing supply and demand. It must be done reliably. It must be done affordably. And increasingly, it must be done in a way that reduces impacts on human health and the environment. In this report, we will mostly focus on reliability and affordability. We will not discuss the effects on human and environmental health of using coal or nuclear power, except to note here that there are many negative effects.

TYPES OF GENERATION—PAST TO PRESENT

In the past, an electricity generation portfolio was created using three types of power plants: Baseload, Intermediate, and Peaker plants. Baseload plants are those designed to meet the “base load” of electrical demand, which is the minimum power demand that can be expected to persist from day to day. These
plants are rarely offline and take days to weeks to start up or shut down. This inflexibility has not been a severe detriment in the past because the plants are meant to supply only the minimum power demand on the system (e.g., weekend nights with moderate temperatures). Baseload plants are typically very large coal and nuclear plants, although hydroelectric, geothermal, biomass, and certain types of natural gas plants can also provide baseload power. In the past, baseload plants operated with relatively high reliability and relatively low operating costs compared with other sources of power.\(^1\)

**Intermediate** (or “load following”) plants are used daily. In contrast to traditional baseload power plants, intermediate plants are flexible enough to vary operations and output. They are used to provide power throughout the most demand-heavy portions of the day. They greatly curtail their operations during low-demand hours like nighttime. Natural gas plants have mainly played this load following role in recent years, particularly natural gas combined cycle (NGCC) plants.

**Peaker** plants are smaller plants that must be able to ramp up and down quickly during peak electricity demand times to ensure reliability in the grid. Peaker plants are typically combustion turbines that burn natural gas or even petroleum (fuel oil). They are not usually used every day at all times of the year. Typically, Minnesota’s gas peaker plants are used at about 2–3 percent of their potential yearly output.

The recent addition of large-scale wind and solar power to the electricity planner’s portfolio means we now have another type of generation resource: **variable power**. As we’ll discuss later, this is contributing to a change in the optimal mix of resource types.

**THE PAST: WHY BASELOAD POWER USED TO BE THE MOST OFTEN CHOSEN TECHNOLOGY**

The first power plant, a coal-fired facility created by Thomas Edison in 1882, served 85 local customers in New York City. Early power plants were small, local power producers, but over the ensuing decades they grew into very large, centralized power plants. This happened for many reasons. Economies of scale reduced the cost per unit of electricity produced. Coal plants required a constant influx of fuel that arrived on trains. The fewer destinations, the lower the transportation costs for a utility. Coal and nuclear plants also need huge sources of cooling water, requiring large infrastructure investments that encourage fewer, larger plants.

The historic trend toward ever larger baseload plants is reflected in Minnesota’s coal and nuclear plants. In Minnesota, the oldest coal units (those built in the 1950s and 1960s) are typically small, between 50 and 100 megawatts in size. The newest coal units, built in the 1970s and 1980s, range between 350 and 900 megawatts in size. The Sherburne County coal plant, Minnesota’s largest and newest coal plant, has three units with a combined capacity of over 2,100 megawatts. Minnesota also has three nuclear units—one at the Monticello Nuclear Generating Plant (631 megawatts) and two reactors at Prairie Island Nuclear Power Plant (each 593 megawatts).

Coal and nuclear plants have always been relatively costly to construct compared with peaker plants on a per megawatt basis, partly because of their size and the inherent dangers and pollution associated with these technologies. That high up-front cost posed less of a financial risk when demand for power was predictably rising. The up-front capital costs could be recouped from ratepayers over many years so that rate shock from these huge investments could be avoided in favor of gradual rate increases over time. Indeed, in earlier decades, power demand grew so fast that planning for supply was fairly straightforward—build large baseload power plants, with huge economies of scale, and let the predictable demand growth catch up to the supply over time.

However, these large, high-cost, long-lived plants can be very risky investments, as the nation learned in the 1970s and 1980s. During that era, utilities around the nation launched massive baseload power plant building projects, assuming that electricity demand would continue rising uninterrupted and that construction costs would stay manageable. Utilities were surprised by (and in many cases ignored) the reduced demand growth associated with the 1973 and 1979 oil crises and the subsequent recessions, dramatically rising construction costs (especially for nuclear
plants), and new safety concerns following the Three Mile Island accident in 1979. As a result, more than 100 nuclear plants and 80 coal plants were cancelled nationwide, sometimes after hundreds of millions of dollars had already been spent. In other cases, plants were completed but represented costly excess capacity for years while waiting for demand to catch up, often as long as 20 years after plants came online. This resulted in lower revenues to pay off the interest on capital, which meant higher price tags for the plants. Legal battles erupted around the nation to determine whether utility stockholders or ratepayers should bear the billions of dollars in losses.\(^2\)

Today, utilities are faced with similar challenges. A recession and an increasingly energy-efficient society are resulting in forecasts of relatively low growth in electricity consumption. The public is increasingly concerned about the health and environmental impacts of fossil fuel use and nuclear power. In addition, new supply and demand-side technologies have become viable alternatives. With so many old coal-fired baseload plants up for refurbishment, this is a critical time to reevaluate the risks and benefits of traditional baseload power plants and to compare them with emerging alternatives.

**BASELOAD PLANTS TODAY: BENEFITS ARE LESS RELEVANT, DRAWBACKS MORE COSTLY**

To recap so far, we list the historical benefits and drawbacks of traditional baseload power plants.

**Benefits:**
- Reliable source of large amounts of electricity
- Low cost of operation (fuel and maintenance) compared with alternatives
- Up-front capital risk had been mitigated by continuous demand growth

**Drawbacks:**
- Inflexible output with long ramp-up times of days to weeks
- Fuel cost risk
- Investment risk
- Health and environmental impacts

In the past, baseload power plants’ benefits of high reliability and low operating cost largely outweighed other concerns about health and environmental impacts. Large up-front investment risk was lessened (with exceptions mentioned earlier) by relatively reliable demand growth and the willingness of state regulatory commissions to assess ratepayers for the costs of excess capacity. Fuel costs stayed relatively low compared with other generation alternatives powered by oil or natural gas. The inability of traditional baseload power plants to ramp up and power down quickly was mitigated with intermediate and peaker power plants. As a result, the electricity service model became centered on baseload power plants. **Today’s world is very different.**

Major trends are combining to make traditional baseload power plants less valuable. These trends are exacerbating baseload power plants’ innate drawbacks and are causing their benefits over the “next best option” to dwindle:

- Renewable electricity generation is becoming more widespread and predictable, and it will be deployed widely in a growing number of states. As a result, the electricity grid of the 21st century will need to pair this variable renewable resource with flexible, agile resources instead of large, slow-moving plants unable to ramp up or down quickly.
- Fossil and nuclear fuel costs are increasing, and power plants are being held accountable for their health and environmental costs. As a result, coal-fired and nuclear power plants are not as economically attractive as they once were.
- Growth in electricity demand is slowing. Whereas in the past, a utility could afford the risk of an enormous capital investment because it could be assured that growth would be consistently high, this is no longer the case. Utility customers are now exposed to more cost risk than before.

**INCREASED RENEWABLES AND BETTER WAYS TO INTEGRATE THEM**

Increasingly, there will be a significant amount of renewable electricity on our electricity grids. Twenty-four states have enacted Renewable Energy Standards (RES) requiring utilities to obtain a gradually increasing percentage of the power...
they sell from renewable sources. Another five states have enacted renewable energy goals. Minnesota’s Renewable Electricity Standard is one of the strongest in the nation, requiring utilities to obtain 25 percent of their electricity from renewable sources by 2025, except for Xcel Energy, which must obtain 30 percent from renewables by 2020. Collectively, these renewable energy policies in the Midwest region will result in 24,000 megawatts of wind energy generation added by 2026. Utilities and grid operators are using new methods of planning and innovative technologies to integrate these more variable resources into the grid.

**Managing Variability**

Variability requires utility planners and grid operators to complement renewable energy output with flexible, agile ways of quickly increasing supply or reducing customers’ electricity demands through pre-agreed upon, voluntary demand response contracts. They are increasingly doing this by deploying fast thermal generation, such as “intermediate” and “peaker” natural gas plants that can be brought online and offline in short periods of time. For example, wind energy coupled with generation from intermediate natural gas plants is proving to be very cost effective and reliable. These fast, agile resources are much better complements to variable renewable generation than traditional baseload power plants, which are slow moving and harder to manipulate.³

In addition, new innovations in “demand response” allow utilities and grid operators to increasingly rely on the ability to reduce customers’ demands for electricity. Demand response utilizes voluntary agreements primarily between industrial customers and utilities in which customers reduce electricity usage during periods of peak demand. Many utilities provide financial incentives to customers participating in demand response programs. When customers’ electricity demands can be quickly reduced through load management techniques, it reduces the need for additional supplies of electricity.

**Reducing Variability**

As we find more effective ways to manage variable generation like wind and solar, we are also developing technologies, tools, and techniques to reduce the variability itself. Innovations in wind, solar, and storage technologies and in grid operation tools and techniques are creating solutions that will help make renewable electricity even more reliable.

Many experts consider utility-scale energy storage to be the key to unlocking the vast potential of variable renewable power. Many techniques are commercially employed in niche applications around the world as utilities and energy companies are innovating to realize the large economic benefits of cost-effective storage. “Pumped Storage Hydroelectricity” is currently the most widely used method, with over 129 gigawatts of capacity around the world. “Compressed Air Energy Storage” is also a promising technology identified as one of the cheaper potential options. There are many types of chemical energy storage technologies (i.e., batteries) that are employed by utilities or companies in special applications. The challenge for the coming decade is to continue improving large-scale storage technologies and for policymakers to identify what policies are needed to create a market and economic opportunity for storage innovators.⁴ As these markets and technologies develop, energy storage will play an expanding role in reducing the variability of the future grid.

**Forecasting and Planning**

Improved methods of forecasting and planning are allowing grid operators to more accurately predict variable electricity output. Studies by institutions including the Lawrence Berkeley National Laboratory show that increasing the geographic diversity of variable generation increases its reliability.⁵,⁶ While the wind may not be blowing in one isolated location, wind is generating electricity in other parts of the region. As we continue to add more renewables across the Midwest and the country, we will see increased reliability on the whole. Regional grid operators will draw power from a geographically and technologically diversified portfolio of variable resources.

**Larger Regional Transmission and Electricity Market Management**

Regional grids are becoming more connected and are able to transmit and optimize power across longer distances. Experts are now beginning to tackle the challenges of interconnecting the country’s regional grids and increasing the reach and capacity of transmission lines, realizing enormous value as the country adds more renewables to the system.⁷

In June 2011, the Midwest Independent System Operator (MISO), which manages the electricity transmission grid and electricity markets across 12 U.S. states (from Pennsylvania to Montana) and Manitoba, announced a new resource designation: Dispatchable Intermittent Resources. This
category will allow wind resources to be “treated like any other generation resource in the market and, for the first time, participate in the region’s real-time energy market. Now wind can automatically be dispatched.”

Using some or all of the innovations and trends listed in this section, regional operators like MISO are quickly developing the ability to manage large volumes of renewable electricity on the grid, which substantially increases the value of these resources to the system. Having more renewables on the grid is spurring innovation to increase reliability and complement the variable nature of wind and solar. These innovations include flexible and fast-moving resources such as natural gas plants, technologies that manage customers’ electricity loads, or other near-term technologies like electricity storage.

In this evolving 21st-century electricity grid, the optimal resources are no longer large, inflexible baseload power plants. In fact, our inability to control the traditional baseload plants’ generation output in a timely manner will become an increasing liability, as noted by Jon Wellinghoff, chairman of the Federal Energy Regulatory Commission:

...[If] you can shape your renewables, you don’t need fossil fuel or nuclear plants to run all the time. And, in fact, most plants running all the time in your system are an impediment because they’re very inflexible. You can’t ramp up and ramp down a nuclear plant. And if you have instead the ability to ramp up and ramp down loads in ways that can shape the entire system, then the old concept of baseload becomes an anachronism.⁹

### Costs Are Rising for Baseload Power, Falling For More Flexible Options

In the past, power from traditional baseload power plants has been viewed as reliably cheap. This reputation is quickly changing.

**Construction.** Construction costs for traditional baseload power plants have always been painfully high. Constructing a mid-sized coal plant today would cost more than $1 billion, and costs to construct a nuclear plant are estimated to exceed $5 billion. The U.S. Energy Information Administration (EIA) estimates that 2011 construction costs for new coal and nuclear plants were 25 and 37 percent higher (respectively) than 2010 estimates, indicating the rapid increase in costs for these projects.¹⁰

During the construction boom of the 1970s and 1980s, construction costs skyrocketed, leading to widespread project cancellations and rate increases for customers. This increase in construction costs was blamed on many factors, including rising commodity costs caused by global demand for building materials, especially from fast-growing China. This trend continues today. Unlike newer and more distributed technologies such as solar and wind, these plants are not in a position to benefit from expanded mass-production and technology improvements. Traditional coal and nuclear plant construction costs will continue to rise, just as solar and wind costs continue to fall due to innovation and economies of scale.

**Fuel.** The other large cost element in traditional baseload plants is fuel. One of the justifications for building coal-fired power plants has been the belief that fuel costs would stay low, but that is increasingly unlikely. Between 2000 and 2010, the price of coal delivered to electric utilities nearly...
doubled, despite the economic slowdown in the final years of that decade. One major factor driving U.S. coal prices higher has been the growing influence of global coal markets. Coal imports in China, India, and Japan have been rising steeply, driving up global coal prices and U.S. coal exports. Coal producers in the Powder River Basin in Wyoming and Montana (the source of almost all of the coal burned in Minnesota) are trying to build new West Coast ports to allow them to export coal to the burgeoning Asian markets. This would put Minnesota coal plants in direct competition with Asian coal plants for fuel and make coal prices increasingly like oil prices—driven by global events and more volatile and hard to predict. The cost of coal as a fuel in the future looks increasingly uncertain and unreliable. By contrast, the fuel for wind and solar electricity production is permanently and reliably free.

Health and Environmental Protections. State and federal governments are increasingly concerned with the costs to human health and the environment caused by traditional baseload power plants. New standards to control mercury, soot, smog, and greenhouse gases and to reduce water and waste pollution from coal plants have been recently finalized or will be released in the coming decade. Coal plants in particular must internalize these health and environmental costs by installing better equipment that reduces pollution. In Minnesota, projected costs to clean up aging coal-fired power plants run into the hundreds of millions of dollars. Ottertail Power estimates that its $500 million clean up at Big Stone I will increase rates by 15 percent. The costs for new nuclear plants have become almost prohibitively high due to the increasing cost of equipment, the reduction in the number of manufacturers, the failure of the federal government to fully develop high-level radioactive waste disposal, safety concerns, siting problems, and long delays due to public opposition. These health and environmental protections, equipment costs, logistical problems, and public sentiment will force traditional baseload power plant producers relying on nuclear plants to internalize costs that they could previously transfer to citizens’ medical bills and environmental clean-up costs. As this happens, the price of producing traditional baseload power from this source will more closely reflect its higher true cost, again reducing its appeal as a cost-effective source of electricity.

The Emergence of Natural Gas as an Alternative. As the price forecasts for coal are increasing, natural gas prices have dropped significantly based on new and substantially higher estimates of domestic U.S. natural gas reserves. The EIA expects natural gas-fired power plants to account for 60 percent of new capacity additions in the U.S. by 2035. One of the chief advantages of natural gas plants is the ability to go from a standstill to generating significant amounts of power quickly. This has always been a useful trait but will become even more important as we continue to move toward a dynamic power grid with greater amounts of variable renewable power.

There are many unresolved concerns about hydraulic fracturing, a method used to force natural gas out of fractured rock, which underlies present supply and price forecasts. These concerns include the impacts on water quality, the potential increased incidence of earthquakes, the use of huge amounts of water, and the risk of leakage of methane—a potent greenhouse gas—during the drilling process. These and other factors may greatly reduce the environmental benefits of lower carbon dioxide emissions from gas-fired power plants. The environmental impacts of these new drilling techniques need to be understood and then mitigated if natural gas is to serve as a widely adopted generation resource.

The costs of reasonable environmental protections from hydraulic fracturing are unknown but will certainly place at least moderate upward pressure on gas prices. There is presently a substantial amount of underutilized natural-gas-fired combined cycle capacity in and around the state of Minnesota that could be used to generate needed power as old coal-fired power plants are retired and/or as large amounts of variable renewable power come into the system. A new combined cycle gas-fired power plant should be able to fully operate 60 to 70 percent of the time, which is at or beyond the average capacity factor for coal plants nationwide in 2009. “Capacity factor” is stated as a percentage and represents the amount of time a plant is actually producing power divided by the amount of time it could produce power if it ran all the time. In fact, new, efficient gas-fired combined cycle power plants in Minnesota and the neighboring states of Wisconsin and Iowa appear to be generating far less electricity than they are capable of producing, with capacity...
factors in the range of 10 to 20 percent. This excess capacity gives the region important flexibility as it transitions to the electricity grid of the 21st century.

**More Risk, Less Benefit.** Traditional baseload power plants are experiencing rising construction, fuel, and health and environmental costs. In contrast, new sources of energy such as wind and solar are seeing downward trending costs due to economies of scale and innovation. They have no fuel risk, and their health and environmental impacts are significantly smaller and therefore less costly than coal and nuclear plants. These trends will continue—in a regulatory world where we plan 20- to 40-year capital projects, they must be incorporated into energy resource decision making.

**SLOWER DEMAND GROWTH EXPOSES COST RISK**

Large, traditional baseload power plants require significant new investments. Utilities and regulators take big risks when they add huge chunks of capacity. In the past, utilities would rely on demand to grow, and until very recently, there was steady and relatively predictable demand growth. As noted previously, utilities have made bad bets that cost their ratepayers and/or taxpayers billions of dollars in wasted investment and capital expense. But the general trend in the past was that over the long haul, a large, expensive power plant would eventually recoup its construction and operation costs. This is no longer necessarily true.

**Demand Growth Dropping.** As shown in the figure above, demand growth has dropped dramatically over the last few decades. The EIA predicts around one percent annual demand growth in the future (through 2035), cutting deeply into the cushion that utilities have relied on to reduce risk in planning and constructing traditional baseload power plants. In late 2011, Xcel Energy revised its demand growth projections to .5 percent annually and Great River Energy mothballed a brand new $440 million (99 megawatt) coal plant because there is not enough demand to justify its use.

**Energy Efficiency Increasing.** One of the main reasons Minnesota and U.S. demand growth has slowed is that consumers are becoming more and more efficient in consuming electricity. Minnesota currently has a goal for utilities to save 1.5 percent of their retail sales on an annual basis through energy conservation programs. Even before the 1.5 percent goal became effective in 2010, Xcel Energy alone estimated that its conservation and efficiency programs had eliminated the need for building nine new medium-sized power plants.

Statewide from 1996 to 2009, energy efficiency programs saved Minnesota utility customers $2.5 billion and did so in a highly cost-effective way: For each utility dollar spent, $2.74 was saved. Not only does energy efficiency save consumers money directly, it reduces future energy demand and thus the need for construction of new power plants. Energy efficiency programs cost far less than building new power plants, particularly traditional baseload power plants. According to a report by ICF International, on average, energy efficiency costs between $.02 and $.05 per kilowatt hour, less than any other form of new energy development. A study by McKinsey and Company identified energy efficiency as a “vast, low-cost resource for the U.S. economy” that could save more than $1.2 trillion through 2020. This savings equates to a reduction in consumption of 9.1 quadrillion BTUs, which is 23 percent of future demand. Other states across the U.S. have recognized the immense money savings and demand reduction potential that energy efficiency holds. For example, Illinois, Indiana, and Ohio have goals in place to reduce electricity use by at least two percent annually through efficiency.
As Minnesotans and Americans continue to accelerate the adoption of energy efficiency improvements, utilities will see lower demand growth than in the past. Utilities and planners are recognizing the implications of this fact: We are no longer in a world where large additions of electricity-generating capacity make financial sense. Instead, incremental additions with smaller price tags that are shaped more tightly to load growth will be the economic winners. This will favor generation options with short construction times that are modular in size so that system planners can react quickly to changes in peak demand. In this new paradigm, the large baseload power plants of the past lose relevance.

CONCLUSION: BASELOAD POWER’S PLACE IN THE GRID OF THE 21ST CENTURY

INFLEXIBLE BASELOAD PLANTS ARE OUTDATED IN THE NEW FAST-MOVING GRID

Grid operators are using new tools to optimize resource use. Innovations in modeling and forecasting combine with a smarter, more interconnected grid to increase reliability of renewables and allows grid operators to flexibly dispatch agile resources to ensure that variable supply meets variable demand. These newer technologies and regional operational tools and techniques are crowding out large traditional baseload power plants while still providing the reliability that customers expect.

TRADITIONAL BASELOAD POWER’S SHORTCOMINGS ARE NO LONGER MASKED BY UNBEATABLY LOW COSTS

Construction costs of large coal-fired and nuclear power plants are constantly rising. Fuel costs for coal and nuclear plants are also rising due to increased demand around the world. States and countries are increasingly holding nuclear and coal-fired power plant operators responsible for the costs they inflict on human health and the environment. Meanwhile, wind and solar costs are decreasing, and natural gas—which is an agile complement to variable renewable resources—has become more affordable and possibly more available for electricity generation, making them more cost-effective options for ratepayers. The argument that nothing can compete with coal on cost is no longer true—in fact, barring new innovations in this mature field, dependence on coal will be a liability to ratepayers as future costs increase.

TRADITIONAL BASELOAD PLANTS ARE BECOMING DRAGS ON THE SYSTEM

The value of traditional baseload power plants is diminishing as the electricity world is innovating. Because of the plants’ enormous size, grid operators require maintenance reserves of large amounts of expensive generation capacity in case these large units suddenly shut down or are taken offline for maintenance. Increasingly, “reserve margins” required by regional grid operators are mostly related to the potential for large plants to fail for one reason or another. One advantage of more modular power plants is that they can stop making electricity without posing big reliability problems to the grid. In today’s world, traditional baseload power plants are no longer the least-risk, least-cost option to provide reliable and affordable electricity service. While some traditional baseload plants will continue to operate, their value is diminishing as rapidly as the electricity world is innovating. These plants will no longer provide the benefits they once did as we move to a more agile, dynamic electricity grid that is more controllable, creates less pollution, and results in lower long-term costs.
1 Capacity factors based on 2010 net generation and summer capacity data from EIA (Existing Generating Units in the United States by State and Energy Source, 2010 and EIA Boiler Fuel Consumption/Generating Unit Net Generation).

2 It should be noted that rate-regulated utilities have a built-in incentive to construct high-capital-cost baseload plants, because the more capital they invest, the higher the “rate base” on which their rates are calculated. This is another reason—beyond the inherent financial risk associated with such large and long-term projects—why regulatory scrutiny of power plant projects is particularly important. After the financial disasters associated with a national wave of ill-fated power plant construction in the 1970s and 1980s, many states, including Minnesota, put in place new laws requiring utilities to engage in transparent long-term resource planning so regulators and the public could better oversee their choices and assumptions. Barbara Freese, Steve Clemmer, Claudio Martinez, and Alan Nogee, A Risky Proposition: The Financial Hazards of New Investments in Coal Plants (Cambridge, MA: Union of Concerned Scientists, March 2011), p. 45. Available online at www.ucsusa.org/assets/documents/clean_energy/a-risky-proposition_report.pdf.

3 Some argue that renewables will require “back-up” generation in excess of what we already have for the current baseload-centered paradigm. In a presentation to the Western Electricity Coordinating Council, researchers from the National Renewable Energy Laboratory concluded that, “The traditional focus of resource adequacy has been, ‘How much installed capacity is needed?’ With increasing generation from wind and solar, the additional question is, ‘What type of capacity is needed?’ Wind and solar do not cause need for additional capacity, but may require a different kind of capacity (more flexible capacity).” Michael Milligan and Jack King, “NREL Variability and Reserves Analysis for the Western Interconnect” (slide 24), October 20, 2011. The presentation is available online at www.nrel.gov/docs/fy12osti/53182.pdf.


6 Northrop Grumman has a model that helps planners optimally place their wind sites to maximize diversity and reliability. Dr. Randall J. Alliss, “Maximizing and Optimizing Renewable Energy (MORE) Power,” presented to the Wyoming Infrastructure Authority spring meeting on March 10, 2011. The presentation is available online at http://wyia.org/wp-content/uploads/2011/05/ralliss_more_power.pdf.


19 Summary of data reported by utilities via the Energy Savings Platform to the Minnesota Department of Commerce, Division of Energy Resources. October 2011.
