

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

In the Matter of )  
)  
PUBLIC UTILITIES COMMISSION )  
)  
Instituting a Proceeding to Review the )  
Power Supply Improvement Plans for )  
Hawaiian Electric Company, Inc., )  
Hawaii Electric Light Company, Inc., and )  
Maui Electric Company, Limited. )  
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Docket No. 2014-0183

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**PANIOLO POWER COMPANY, LLC'S PRELIMINARY COMMENTS ON  
THE HECO COMPANIES' POWER SUPPLY IMPROVEMENT PLANS**

KEVIN J. LIPSON  
ANDREW L. SPIELMAN  
HOGAN LOVELLS US LLP  
Columbia Square  
555 Thirteenth Street, NW  
Washington, DC 20004  
Telephone: (202) 637-5614  
Email: [kevin.lipson@hoganlovells.com](mailto:kevin.lipson@hoganlovells.com)  
[andy.spielman@hoganlovells.com](mailto:andy.spielman@hoganlovells.com)

Attorneys for PANIOLO POWER  
COMPANY, LLC

DEAN T. YAMAMOTO  
CARLITO P. CALIBOSO  
TYLER P. McNISH  
YAMAMOTO CALIBOSO  
A Limited Liability Law Company  
1099 Alakea Street, Suite 2100  
Honolulu, Hawaii 96813  
Phone No.: (808) 540-4500  
Facsimile No.: (808) 540-4530  
Email: [dyamamoto@ychawaii.com](mailto:dyamamoto@ychawaii.com)  
[ccaliboso@ychawaii.com](mailto:ccaliboso@ychawaii.com)  
[tmcnish@ychawaii.com](mailto:tmcnish@ychawaii.com)

Attorneys for PANIOLO POWER  
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PANIOLO POWER COMPANY, LLC, a Hawaii limited liability company ("Paniolo Power"), through its counsel, Yamamoto Caliboso LLLC and Hogan Lovells US LLP, hereby submit these comments to the Power Supply Improvement Plans ("PSIP") filed by Hawaiian Electric Company, Inc. ("HECO"), Hawaii Electric Light Company, Inc. ("HELCO"), and Maui Electric Company, Limited (collectively, the "HECO Companies").

**I. INTRODUCTION AND BACKGROUND**

Parker Ranch, Inc. is one of the largest and oldest cattle ranches in the United States. The ranch operations encompass approximately 130,000 acres and spans over 7,000 feet of elevation change. The economic prospects of Parker Ranch, Inc. and the competitiveness of the surrounding communities have been severely affected by the high price of electricity and the high cost of living.

In September 2013, Parker Ranch, Inc. began a comprehensive analysis of its resources with a consortium of partners including Siemens, Booz Allen Hamilton, and Pace Global. The efforts focused on Parker Ranch, Inc.'s overarching goal of developing

a compelling, competitive plan to transform the Big Island energy landscape over the next 10 years.

Paniolo Power, a subsidiary of Parker Ranch, Inc., was established in April 2014 to promote and pursue community-level, regional-scale and island-wide clean energy solutions to address high energy costs and seek reasonably-priced clean energy for the Waimea and Kohala communities and, possibly, the entire Big Island.

Paniolo Power filed its Motion to Intervene in this docket analyzing the PSIPs on August 27, 2014 with the intent to:

1. Advocate for the identified range of competitive energy generation and grid portfolio options that can be developed for the benefit of the communities in and around Waimea and North Kohala and the Big Island as a whole;
2. Address the detrimental impacts of prolonged high electricity rates outlined in the PSIPs on legacy and new operations and businesses, and take action to reduce those impacts through solutions that will reduce rates in the near term; and
3. Call attention to the inherent interdependence of rising electricity costs and the economic competitiveness, agricultural productivity, and long-term sustainability of Hawaii's communities.

## **II. PANIOLO POWER'S COMMENTS TO THE PSIPS**

In response to Order No. 32294, Inviting Public Comment on the HECO Companies' Power Supply Improvement Plans, issued on September 12, 2014 by the Hawai'i Public Utilities Commission, Paniolo Power respectfully submits the following comments.

**A. Unique Opportunity in the Economic History of Hawai'i to Advocate for Change.**

Certain periods in history are most notable because of the leadership required to facilitate real change. Paniolo Power views this opportunity to advocate for change as unique in the economic history of Hawai'i.

Paniolo Power recognizes the leadership demonstrated by the Commission in seeking transformational change by soliciting input from the public at large, as well as private interests affected by Hawaii's excessive exposure to oil. Paniolo Power was inspired by the Commission and applauds it for opening these important dockets to review the PSIPs of the HECO Companies and consider the "Future of Hawaii's Electric Utilities".<sup>1</sup>

Nearly every aspect of our society has been touched by the dramatic rise in the prices of energy and electricity. The impacts of these external forces are felt by nearly all businesses and consumers. Society could argue that more could have been done in recent years by business leaders and policymakers to anticipate and counteract these impacts. It could also be argued that resources, especially non-renewable resources, are not sufficiently understood in terms of the extent of reserves, the true costs to society, and the rates of consumption. These largely unquantified unknowns and uncertainties mean society assumes many risks in relying on any particular resource for its needs. Additional risks are assumed when these resources are imported instead of cultivated from domestic sources.

The diverse set of indigenous resources immediately available to the people of

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<sup>1</sup> Commission's Inclinations on the Future of Hawaii's Electric Utilities: Aligning the Utility Business Model with Customer Interests and Public Policy, Exhibit A to Decision and Order No. 32052, filed April 28, 2014, in Docket No. 2012-0036.

Hawaii should be comprehensively evaluated to understand how they may be cultivated for both energy and food. Locally-based commercial scale agricultural must be profitable in the long run in order for sustainability to be established and maintained. Today's energy and electricity prices essentially preclude many forms of commercial scale agriculture from achieving profitability.

The rise in the cost of living is thwarting Hawaii's economic growth potential and development opportunities. This is a unique opportunity to advocate for an alternative energy strategy to benefit our society. Certain costs should be expected in adopting an alternative strategy. These costs are likely to come in the form of new capital investment and potentially stranded assets.

However, those costs are likely to be worth incurring in exchange for a more progressive and aggressive plan to adopt renewable energy and lower electricity prices. A transformational plan executed over a more reasonable timeframe would likely produce benefits that far outweigh the costs. Paniolo Power believes that the Big Island should be the beneficiary of capital investment in a new and alternative energy strategies because electricity rates are the highest for its residents and businesses.

To ensure economic viability and growth potential, large-scale customer defection seems most likely to occur on the Big Island because its electricity rates are the highest and its endowment of natural resources for energy is the greatest in both absolute and relative (e.g., per capita) terms. A more aggressive timetable for transforming the entire system could prevent large-scale grid defection.

A legitimate plan to transform the energy sector of Hawaii's economy should rethink the business strategy of the utility, redefine the utility's business model, and adopt a

transformational capital plan as well as accomplish these objectives in less than 10 years.

**B. Unique Opportunity to Rethink the Business Strategy of the Utility.**

A new and alternative business strategy often requires new ways of thinking strategically and translates into new ways of prioritizing capital investment. It seems clear that new investment possibilities are emerging in both transmission and distribution as well as generation. These new opportunities to deploy capital in the electric utility sector should be evaluated and prioritized simultaneously. It is reasonable that the utility recover its investment and earn a fair return over time. However, ratepayers should benefit in the near-, medium- and long-term.

The business strategy of the incumbent utility should be assessed from at least two vantage points: (1) the ability to attract and retain interest from sources of capital to achieve and maintain a sustainable business model, and (2) the ability to provide safe, reliable, and affordable power to society as a whole. Paniolo Power believes the opportunities to attract and invest capital in a way that meets both of these criteria are abundant and unprecedented, both on the transmission and distribution side of the business as well as on the generation side. Paniolo Power also believes that new capital will benefit consumers, especially given the advancements in technology and the falling cost curves for renewables.

A primary concern for Paniolo Power is balancing the new investment by the utility and third-parties against the potential benefit to consumers. The PSIPs appear to rely on third-party capital as a significant source for new investment in generation over the next 20 years. Yet the PSIPs seem to indicate the utility is prioritizing investments in the grid in the near-term without any clearly articulated justification in terms of near-term rate benefit.

Indeed, the benefits to ratepayers from new cleaner generation appear to be deferred well into the future. Moreover, a plan relying significantly on outside private interests and third-party capital is not really a plan per se.

The thinking reflected in the PSIPs appears linear and incremental instead of strategic and transformational. The apparent sequencing of investments over 20 years reflects a change in priorities – shifting investments to the grid and relying on third-party capital for new generation in the far distant future. It is interesting to note that resources are included in their plans in the future that are apparently not even proven. These uncertainties surrounding the makeup of future generation will likely need to be pursued and addressed by private interests seeking to cultivate cleaner and cheaper sources of energy for Hawai'i. It seems that the strategy of accelerating the adoption of an alternative generation plan will likely also need to be led by other private interests.

Unfortunately, the utility's PSIPs also appear to assume that electricity rates are currently affordable, which, for many reasons, is not the case. Rate relief appears not to be a near-term objective of the plans. If relief from high electricity rates were among the utility's highest strategic priorities, investments on the Big Island would be frontloaded in their capital plans.

Paniolo Power believes the plans should exhibit the prioritization of investments that benefit consumers, not just the apparent prioritization of growing the balance sheet and increasing the enterprise value of the incumbent utility.

### **C. Where is the Utility Business Model Transformation?**

A serious re-evaluation of the utility's business model would and should have contemplated the merits of the complete separation of transmission and distribution

("T&D") from generation. In addition, the utility does not appear to have contemplated or have made a cogent argument regarding the merits of remaining a vertically integrated monopoly that retains ownership and control of both T&D and generation.

It seems that a compelling alternative business model would separate T&D from generation, and either:

1. entrust dispatch to the transmission provider; or
2. effectuate a regulatory policy change resulting in an independent system operator controlling dispatch.

This would help to ensure that the potential financial conflicts of interest of the same company owning T&D and generation would not become real conflicts and possibly harm ratepayers. A complete separation should also reduce the likelihood of circumstances arising where shareholder interests are prioritized at the expense of ratepayers.

It seems that the serious transformation of the utility business model would explicitly trigger the contemporaneous separation of T&D from generation, recognizing that the ownership and management (i.e., dispatch) of these assets could and probably should be separated to ensure the interests of the ratepayers are protected and promoted. The business model is not really transformed without the essential element of ending the vertically integrated monopoly in the near future.

**D. Lowering Rates for All Should be Our Highest Strategic Priority.**

If lowering rates as soon as practical were the primary objective, capital would be invested in utility-scale renewables sooner rather than later as suggested by the utility's PSIP. The proposed utility reforms to net metering will slow the adoption of rooftop solar. Yet not everyone can afford rooftop solar and would be affected by these proposed



reforms. A higher priority should be assigned to initiatives that would benefit all consumers and businesses, not just the subset that possess the motivation, credit score and financial wherewithal to adopt rooftop solar and other possible residential solutions. A plan for reducing rates should place at least equal emphasis on prioritizing utility-scale solutions in order for as many residents to benefit as possible.

**E. Adopting a Resource Optimization Approach for Potential Renewable Energy is Imperative.**

Each island would benefit from a resource optimization approach to prioritizing investments in generation. For example, the capacity factor for solar is highly dependent on the micro climate of a given neighborhood or town. The ideal locations for possible utility-scale solutions are also unique across the islands. The capacity factor of winds in the area of Kohala on the Big Island, for example, are substantially higher than the capacity factor for solar.

These factors, along with a systems thinking approach, should be considered in combination with available land and land cost factors to develop an optimal land use strategy for utility-scale renewables on an island by island and statewide basis. As previously stated, the integration of new utility-scale renewables should be prioritized to achieve the goal of lowering rates for all. It remains unclear why the plans selected by the HECO Companies are their preferred plan versus other possible scenarios.

**F. The PSIPs Fail to Assess the Risks of Large-Scale Grid Defection.**

The cost of renewables is sufficiently compelling for regions and communities to consider leaving the incumbent utility's grid altogether. The efforts of Siemens on behalf of Parker Ranch, Inc. included evaluating the merits of a "community microgrid" demonstrating the viability of an alternative solution to providing the community with

electricity which could lower rates whether the utility's power lines were used or not. The study also suggested that the proportionate share of fixed costs otherwise shifted to the remaining customers could be absorbed in the form of a "departure fee" to compensate the utility for its fixed and otherwise potentially stranded costs. The potential for mass grid defection should motivate the utility to produce more aggressive and meaningful plans. If not, capital is likely to flow to the alternative energy strategies that circumvent the control of the incumbent.

**G. An Optimal Systemwide Allocation of Capital Should Result in Better Rates and Returns.**

Paniolo Power has observed that the Hawai'i Electric Light Company, Inc. (HELCO) on the Big Island has among the lowest regulated return of the HECO Companies (HECO, MECO, and HELCO). Yet, the Big Island suffers from the highest rates (\$0.42/kWh).<sup>2</sup>

The comparative low rate of return and the high price of electricity seem entirely inconsistent. The transition to renewables on a system-wide basis should result in lower electricity rates and arguably higher rates of return, especially if customers would be retained and defection could be avoided. This implies poor capital allocation if both potential returns and rates were factors in deploying capital across the islands. As previously stated, it would seem that the capital plans of the utility would prioritize investments on the Big Island since the rates on the Big Island are the highest.

Alternatively, it suggests that the utility has not included a serious evaluation of the possibilities in generating electricity from renewable sources in its own planning methodology. It also implies the rates of return on T&D are substantially lower than the

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<sup>2</sup> Department of Business, Economic Development & Tourism, Monthly Energy Trends, September, 2014, available at <http://dbedt.hawaii.gov/economic/energy-trends-2/>.

rates of return on generation investments.

#### **H. T&D Costs Appear High on the Big Island.**

As part of the analysis conducted by the Siemens team, Pace prepared an analysis of what a hypothetical wheeling rate (per kWh) would be. Using the recent HELCO 2012 rate case filings<sup>3</sup>, a thorough analysis indicates that approximately \$0.12/kWh of the \$0.42/kWh comes from T&D costs, which exceeds the national average for total electricity cost, including T&D and generation, at \$0.11/kWh.<sup>4</sup> How is it possible that the implied cost of using power lines (just T&D) to deliver power on the Big Island exceeds the national average cost for electricity? The utility should explain the apparent high implied cost of T&D with benchmarking costs vs. utilities elsewhere.

#### **I. HECO or the PUC Must Analyze Liquefied Natural Gas (LNG) Strategies.**

The legitimacy of an LNG strategy should be based on, at least in part, the renewables enabled by using natural gas, not just the marginal benefit of switching fuels. Importation of LNG in bulk seems more economical than in mass numbers of ISO containers. The HECO Companies' strategy seems not to be the lowest cost option given other available choices. The best option for the ratepayer should be pursued since the investment in the necessary infrastructure would affect ratepayers for many years into the future. A bulk strategy utilizing the existing infrastructure in place owned by Hawaii Gas would seem to offer a legitimate lower cost alternative. In addition, the lack of a cogent argument for the utility to remain a vertically integrated monopoly would suggest that the LNG infrastructure should be owned and controlled by an entity other than the electric

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<sup>3</sup> HELCO's "Application for Approval of Rate Increases and Revised Rate Schedules and Rules," filed May 1, 2012, in Docket No. 2012-0099.

<sup>4</sup> U.S. Energy Information Administration data, available at <http://www.eia.gov/state/?sid=HI>.

utility.

**J. Oil Should be Replaced by Diversified Portfolios of Generation, Not Just LNG.**

The near term priorities of the utility seem focused on net metering reform and the adoption of LNG. It seems that replacing the oil-fired generation across the State of Hawai'i is sensible given today's expectations for oil prices. However, the abundance of potential indigenous resources available to generate electricity at more compelling rates should inspire the utility to adopt diversified portfolios of renewable generation instead of deferring them to many years in the future. Mere conversion of power plants from oil to LNG seems shortsighted.

**K. The Big Island Has Not Been Prioritized, Despite Suffering the Highest Rates.**

It would seem logical for the utility to prioritize the implementation of "transformative" solutions and deployment of capital to address the market where rates are the highest and the "economic pain" is greatest -- on the Big Island. HELCO's electricity rates on the Big Island are the highest in the nation, when compared to the other States, and among the highest of any utility in the world. No other Investor Owned Utility (IOU) in the United States comes close to HELCO's electricity rates at \$0.42/kWh. (The next closest state is New York at an average of \$0.21/kWh.)<sup>5</sup>

Yet the Big Island economy is perhaps more sensitive to high electricity rates than the economies of the other counties. With a large portion of the population living in rural areas and employed in a concentrated set of sectors tied to tourism, services, and agriculture, Big Island wage growth has been stagnant and not kept pace with the rising

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<sup>5</sup> U.S. Energy Information Administration data, available at <http://www.eia.gov/state/data.cfm?sid=NY>.

cost of living. In fact, 25% of the Big Island is on food-stamps, the highest of all the counties.<sup>6</sup> The high cost of living forces many families to make difficult decisions about whether to keep the lights on or pay for food, medicine, healthcare, or other necessities. If rates were adjusted for the cost of living compared to Oahu, the \$0.42/kWh rate would reflect the higher disproportionate burden electricity costs have on businesses and citizens on the Big Island. Hawaii's economic competitiveness has suffered, causing import substitution and other sustainability strategies to face headwinds difficult to overcome.

The HECO Companies, however, report that renewable energy generation on the Big Island accounts for 48% of total electricity sales, and count this HELCO renewable portfolio standard (RPS) in their blended HECO Companies RPS, bringing their overall total RPS to 18%, just above the HCEI 2015 goal of 15%.<sup>7</sup> Without the Big Island RPS in the equation, the combined RPS of the HECO and MECO generation portfolios would fall well short of meeting the HCEI mandated RPS targets.

Despite the pain that the HELCO customers have endured with rates over \$0.40/kWh since early 2011, the utility has not prioritized solutions to lower rates on the Big Island within the next 10 years in its PSIP. While HELCO will likely point to the oil-tied avoided cost contracts HELCO executed with renewable energy independent power producers' (IPPs) when the price of oil was much cheaper (and the contracts made economic sense), there is little excuse for the consistent failure to prioritize and explore

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<sup>6</sup> State of Hawaii, Department of Human Services, SNAP Participation Rates Archives, <http://humanservices.hawaii.gov/bessd/snap/>

<sup>7</sup> Hawaiian Electric Industries, Inc. Financial Community Meetings Company Overview Presentation, dated March 18-20, 2014, available at <http://phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9MjI1NTU3fENoaWxkSUQ9LTF8VHlwZT0z&t=1>

new solutions on the Big Island to lower rates.

**L. The Incumbent Power Provider Has Not Advanced a “Transformational” Plan.**

A “transformation” in the corporate world normally occurs over a period of a few years and very rarely takes as long as 10 years. For example, the transformation of IBM from a desktop PC maker to a global technology solutions company took fewer than 10 years. In another example, just this year (2014), Burlington, Vermont, the largest city in the State of Vermont, with a population of 42,000, announced it would be able to produce 100% of the city’s electricity with renewable energy, further evidence of the potential for “real” transformation that is possible.<sup>8</sup> The most significant elements of the PSIPs which benefit ratepayers appear to occur after 10 years have elapsed. This lack of a sense of urgency casts serious doubt on the legitimacy of these plans as a sincere attempt to “transform” the electricity sector of the Hawaii economy. The sheer amount of time suggested by the incumbent utility will cost the economy while it continues to suffer from excessively high rates. It is unclear why the new investments in generation -- especially utility-scale generation -- are delayed for many years when the rewards could begin accruing to the benefit of all residents and businesses sooner if they were accelerated.

**M. Transformational Ideas Would Attract Transformational Capital.**

Transformational capital is needed to transform the energy landscape of Hawai’i. In the very near future, Hawai’i needs to make a shift in its strategic posture and positioning. Hawai’i needs to import capital for investing rather than import oil for burning. The capital required to transform the energy landscape in Hawai’i is substantial – in the billions of

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<sup>8</sup> Wilson Ring, “100% of power for Vermont city now renewable,” The Boston Globe, September 15, 2014, available at <http://www.bostonglobe.com/metro/2014/09/14/vermont-milestone-green-energy-efforts/fsLHJl4eoqv6QoFNewRYBK/story.html>

dollars. These investments are warranted to avoid importing fossil fuels, to adopt renewables more aggressively, and to protect the environment by significantly reducing carbon emissions, while also reducing electricity rates. The Hawai'i Clean Energy Initiative estimated that the net benefits of scenarios including large-scale renewables far outweigh the capital tied up in generation assets of the utility at current levels of oil prices. A significant portion of the capital necessary for a transformation will need to be imported. Transformational sources of capital seeking investment opportunities prefer certainty and a reasonable time horizon. A more clearly delineated plan with a time horizon of 5 to 7 years would be more beneficial to attract transformational capital.

**N. The Time Value of Money, the Cost to the Utility and the Benefit to Society.**

The longer the amount of time any transformation requires, the smaller the value of the net benefit of the transformation to the intended beneficiaries, all other things being equal. Aside from the benefits derived from the actions taken pursuant to a transformation, the time value of money is likely a primary determinant of the magnitude of the benefits. With this in mind, two key interconnected questions are essential to contemplate:

1. What is the cost to the utility of accelerating a transformation?
2. What is the benefit to society of accelerating a transformation?

The more accelerated a transformation, presumably the larger the cost to the utility and the larger the benefit to society. In a sense, then, the crux of the matter is really a question of social costs and benefits.

An accelerated transformation would be presumed to be “costly” to the utility because the utility did not incorporate a more rapid transition into their plans. If it were

beneficial to the utility, presumably they would have included a more rapid transition in their plans. This seems a reasonable assumption given the time and effort invested in developing the plans on their part, unless there is an oversight or shortcoming in their planning process.

The social benefits of the plan to the ratepayers seem way too far into the future. The value to society of the plans is diminished because of the time that elapses between now and when net benefits begin to accrue. A dollar is more valuable today than ten years from now, because (among other things) a dollar received today could earn compound interest for ten years, yielding much more than a dollar ten years from now. In the same fashion, accelerating the plan should enhance the magnitude of the net benefits that accrue because they would occur sooner.

The larger the benefit to society, the more benefit available to absorb the cost to the utility of the possible decision to accelerate a transformation. What could be the cost to the utility?

The social benefits could very well exceed the costs to the utility. The cost to the utility would depend, at least in part, on what costs were not covered by the ratepayers. In theory, the utility should be motivated to accelerate the transformation to avoid large-scale customer grid defection. The ratepayer might be willing to absorb some, most or even all of the cost of accelerating a transformation, especially if the benefits were seen much sooner than otherwise reflected in the utility's PSIP. The benefits to society should be thoroughly examined for what could be real and realized sooner.



### **III. CONCLUSION**

In summary, the utilities' monopolistic tendencies appear to be reflected in the PSIPs, including lack of innovation and transformational investment, especially when compared to the strides and progress towards transformation of the other utility in the state, Kauai Island Utility Cooperative (KIUC).

It is also apparent to large landowners that land values, including agricultural land, and opportunities to harness resources for greater sustainability and self-reliance in terms of food, energy, and water, are greatly affected by high electricity rates.

Paniolo Power and Parker Ranch, Inc. will vigorously pursue all regulatory remedies to ensure that Hawai'i ratepayer interests are at the forefront of regulatory initiatives. Society, it seems, would benefit from a more progressive and aggressive transformation of the electricity sector within a more relevant and meaningful time horizon.

Respectfully submitted on October 6, 2014.



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DEAN T. YAMAMOTO  
CARLITO P. CALIBOSO  
TYLER P. McNISH

YAMAMOTO CALIBOSO  
A Limited Liability Law Company  
1099 Alakea Street, Suite 2100  
Honolulu, Hawaii 96813  
Phone No.: (808) 540-4500  
Facsimile No.: (808) 540-4530  
Email: [dyamamoto@ychawaii.com](mailto:dyamamoto@ychawaii.com)  
[ccaliboso@ychawaii.com](mailto:ccaliboso@ychawaii.com)  
[tmcnish@ychawaii.com](mailto:tmcnish@ychawaii.com)

KEVIN J. LIPSON  
ANDREW L. SPIELMAN

HOGAN LOVELLS US LLP  
Columbia Square  
555 Thirteenth Street, NW  
Washington, DC 20004  
Telephone: (202) 637-5614  
Email: [kevin.lipson@hoganlovells.com](mailto:kevin.lipson@hoganlovells.com)  
[andy.spielman@hoganlovells.com](mailto:andy.spielman@hoganlovells.com)

Attorneys for PANIOLO POWER COMPANY,  
LLC