

INVESTIGATION OF RESOURCE ADEQUACY ALTERNATIVES

BPU DOCKET NO. EO20030203

REPLY COMMENTS OF THE NEW JERSEY LARGE ENERGY USERS COALITION

“It was all very well to say ‘drink me’, but the wise little Alice was not going to do that in a hurry. “No, I’ll look first”, she said, “and see whether it’s marked ‘poison’ or not.”

Lewis Carroll
Alice’s Adventures in Wonderland

The New Jersey Large Energy Users Coalition (“NJLEUC”) appreciates the opportunity to offer these Reply Comments regarding the Board’s investigation of resource adequacy alternatives in response to the Minimum Offer Price Rule (“MOPR”) Order issued by the Federal Energy Regulatory Commission (“FERC”). NJLEUC incorporates by reference its Initial Comments in this proceeding, which were submitted on May 20, 2020.

D). Overview

In our Initial Comments, we indicated that we fully share the Administration’s frustration with the MOPR and other Federal actions that could impede implementation of the State’s energy policies and, in particular, the clean energy goals of the Governor’s Energy Master Plan. As we noted, this is not the only example of dissonance between State and Federal energy policies, as such incidents have now occurred in several instances spanning more than a decade.

However, we continue to urge the Administration not to allow the frustration of the moment to persuade the State to depart the PJM capacity markets and to adopt the Fixed Resource Requirement alternative (“FRR”) available under the PJM tariff. For a deregulated state like New

Jersey, adoption of FRR would entail the partial re-regulation of the electric generation function through a largely untested device fraught with unintended consequences and potential financial and other risks that could vastly overshadow FRR's limited benefits. We rely on the extensive treatment of these issues and risks set forth in our Initial Comments and will not repeat them here.

We do note, however, that our Initial Comments assumed that PSE&G would be the most vocal proponent of FRR and the joint comments filed by PSEG (not PSE&G) and Exelon Generation (not Exelon Corporation) have proven us right. What was not expected was that the Companies would come forward with their own, more expansive, FRR proposal, which will be discussed at length in these comments.

More importantly, what was quite surprising is the almost complete absence of stakeholder support for FRR. In fact, the myriad of environmental, solar and offshore wind groups and businesses that filed comments—the companies that would be the presumed beneficiaries of an FRR regime—each articulated a host of concerns about the potential for exercises of market power to increase capacity costs, a variety of cost responsibility, policy, competitive and legal issues, and the potential for unanticipated consequences that could result from adoption of FRR. Each of these commenters urged the Board to consider and pursue other alternatives, such as implementing carbon pricing or conducting negotiations with PJM to soften the impact of the MOPR.

So why do PSEG, the Public Service Enterprise Group holding company that includes PSEG Power (“PSEG”), and Exelon Generation, the generation affiliate of Exelon Corporation (“ExGen”), (collectively “the Companies”) support FRR? This is an interesting question given that their support for FRR comes hard on the heels of the adoption of the ZEC Law, which provides the Companies \$300 million in annual subsidies for their New Jersey nuclear plants. So it is certainly fair to ask: why are the Companies so willing to give up their hard-won ZEC subsidies if

their FRR proposal is adopted? The obvious answer is that the Companies perceive a substantially larger business opportunity available to them by exploiting the Administration's frustration with FERC, PJM and the MOPR and desire to consider alternatives—a cause the Companies have been quick to embrace.

The phenomenon is commonly known as “wrapping oneself in the flag”. The phenomenon occurs where an opportunistic party seizes upon a matter of great public interest—here, the investigation of clean energy-friendly alternatives to the MOPR—and, while professing to act in the public interest, in reality acts in a manner that supports a motive that is selfish in nature, intended to advance the party's interests, rather than those of the public. Thus, the Companies' comments contain a proposal for a clean energy procurement regime that goes far beyond the mere adoption of FRR, a mechanism designed to enable a state to assert greater control over its capacity procurement policies outside of the RPM auction and Federal regulation.

Rather than simply supporting the FRR procurement model as defined by PJM, the Companies instead propose an unsolicited and expansive “Integrated FRR Procurement” methodology. The Companies state that the methodology, which they acknowledge is not authorized by current law, would facilitate the State's desire to expand its clean energy resources, by “integrat(ing) the procurement of capacity with the procurement of environmental attributes.” The “integrated” procurement would enable the State to purchase clean energy resources at an all-in price fixed at the outset of long-term bilateral contracts. The Board would “oversee” the procurement process and set a ceiling “all-in” price for the capacity and environmental attributes. (Companies' Comments at 3). Under the Companies' proposal, the procurement of favored clean energy resources would be accelerated by their inclusion in a “Tier I” procurement that would prioritize the development of clean energy resources mandated by the Energy Master Plan.

(Companies' Comments at 4). The selected FRR Entity would fill as much of the tier as possible with the resources targeted by the MOPR—e.g. offshore wind, new grid-connected solar projects and nuclear resources. Once the zone approaches 100% clean capacity, the Board would select a second utility to become an FRR Entity for a second tier encompassing the second utility's zone, and so on. (Companies' Comments at 7).

The Companies argue that their approach would permit the State to control its energy destiny and “fully and timely achieve its EMP goals at a lower cost for consumers than they would otherwise pay by avoiding the inefficiencies that will result from FERC's new bidding rules in the PJM capacity auction”. (Companies' Comments at 4). By these and other similar statements in the Comments, the Companies present their Integrated FRR Procurement methodology as a necessary and logical component of the State's clean energy efforts that is compatible with the State's restructured competitive retail markets and the BGS auction.

Surprisingly, the Companies offer, without explanation, to abandon the ZEC program if the Board adopts the “Integrated FRR Procurement Methodology” proposed by the Companies. (Comments at 3). Clearly, the Companies' proffer should set off alarm bells and red flags. One must seriously question what it is about their proposed “mechanism” that would prompt the Companies to so readily forego the ZEC program, a program that provides the Companies with \$300 million a year in subsidies, and for which the Companies fought so hard in a two year legislative battle and an intense BPU process. What indeed? It should be evident that the Board must investigate not only whether the Companies' “mechanism” is a viable method to advance the State's clean energy goals, but also the extent to which the mechanism would favor the Companies' own financial interests to the detriment of ratepayers, the BGS auction and the competitive marketplace.

The answer may be found by analyzing how the Companies' proposed Integrated FRR Procurement Methodology would likely work in practice. As will be addressed at length below, because there are currently only limited solar and wind resources available to participate in the proposed "Tier I" procurement, the procurement would clearly be dominated by the Companies' Salem I and II and Hope Creek nuclear plants, which are considered "clean energy" for purposes of such procurements. The dominance of the nuclear units would be expected to continue for an extended period as the desired solar and wind resources are merely in their incipient stages of development and will occur gradually over time. The scope of the procurement would also be further limited by FRR rules that require the use of localized capacity resources within the FRR zone and the existence of chronic transmission constraints that restrict imports of power.

As a result of these factors, the FRR procurements will largely be limited to capacity located in the delivery zone of the EDC selected as initial "FRR Entity" and the larger Eastern MAAC zone. Therefore, given the minimal renewable resources currently available, each of the Companies' proposed procurements would be dominated by their New Jersey nuclear stations, as well as the Limerick (ExGen) and Peach Bottom (PSEG/ExGen) stations located in Eastern Pennsylvania and, potentially, the Calvert Cliffs (ExGen) station in Maryland.

Under the Companies' proposal, their nuclear plants would be removed from the PJM competitive capacity market, where they are subject to a host of bidding rules, consumer protections and monitoring by the PJM Independent Market Monitor ("IMM"). The units would be remanded to a highly concentrated FRR capacity marketplace that would not have the market rules or oversight currently provided by PJM, and in which the Board would be responsible for planning capacity resources, oversee procurements and, through an unspecified procedure,

establish ceiling prices for the capacity and environmental attributes being procured by the FRR Entity.

In reality, the components of the Companies' proposed Integrated FRR Procurement Methodology are singularly inconsistent with the Electric Discount and Energy Competition Act ("EDECA") and would result in the *de facto* re-regulation of the Companies' nuclear plants. Because there is no suggestion in the Companies' proposal that the prices for capacity and environmental attributes would be established through a competitive procurement or a contested proceeding designed to result in just and reasonable rates, there is a clear potential for the arrangement to again provide windfall profits to the nuclear plants, particularly given the Companies' significant market power in New Jersey and Eastern MAAC. Would the proposal result in another ZEC situation in which Ralph Izzo provides the number that is "needed" to provide PSEG with an "acceptable" rate of return for the nuclear plants? Would the Board set the FRR ceiling prices in ZEC-like fashion, denying "non-essential" parties access to the "commercially sensitive" information that would provide the basis for the "all-in" prices sought by the Companies?

The Companies' argument that their preferred FRR method would result in customer savings is belied by the experience of FRR entities in states like Ohio, Virginia and Michigan, where companies like AEP have leveraged FRR to obtain capacity prices significantly higher than those established in the PJM BRAs. In this regard, it is noteworthy that in its otherwise benign comments, PJM provided the following advice to the Board: "PJM does not comment with respect to the cost of an FRR for New Jersey. Instead, PJM cautions the BPU to look critically at any outright claims offered at this point in the proceeding that an FRR *will* prove less expensive for New Jersey consumers". (PJM Comments at 17) (emphasis in the original).

The notion that the Companies would forego \$300 million in annual ZEC subsidies and instead offer customers discounted capacity prices and reasonable costs for the environmental attributes associated with their generation is one worthy of Alice in Wonderland. Rather, it is far more plausible that the Companies will obtain higher profits through their FRR proposal and secure a back door form of re-regulation that would improperly shift operational and performance risks to customers that should be borne by shareholders and result in rates that are not just and reasonable. Of course, no thought is given to returning the \$3 billion in stranded costs paid by ratepayers as the price for deregulation.

Adoption of the Companies' proposal would also allow them to conveniently avoid the close scrutiny that clearly awaits them in the upcoming ZEC Phase II proceeding, in which the amount of the ZEC subsidy, if any, that would be payable to the Companies in future delivery years will be very much an issue. There should be little doubt that the Companies would prefer to institutionalize and lock these payments into rolling long-term capacity/environmental attributes contracts procured under the rules they propose rather than face scrutiny that likely would confirm what Board staff and a number of experts said all along—that the nuclear units are covering their costs and don't need to be subsidized.

Although the MOPR Order is on appeal in both the D.C. and Seventh Circuit Courts of Appeal and could well be overturned, particularly if there is a change in administration in Washington, the Companies nonetheless urge the Board to quickly adopt their proposal, ostensibly so that the State's energy initiatives can proceed expeditiously. The argument for haste in adopting the Companies' highly questionable proposal is what brought the Alice in Wonderland quote to mind. NJLEUC urges the Board and Administration to take its time, and carefully read "the label"

attached to the Companies' proposal—regardless of how attractive it may appear at first blush--to avoid drinking what could well be revealed to be regulatory “poison”.

II). Analysis of the Companies' Proposed Integrated FRR Procurement Methodology

A). Market Power

It is surprising and ironic that PSEG and Exelon Generation elected to file joint comments in this proceeding, and the irony should not be lost on the Board. These are the same companies whose proposed merger in 2005 set off a fire storm of opposition due to the unprecedented market power the combined company could have wielded in New Jersey, EMAAC and PJM generally. The merger was ultimately rejected by the State and stakeholders due to the Companies' steadfast refusal to divest any of their expansive generation fleet, and in particular the nuclear plants, which prompted widespread concern that the Companies would leverage their considerable market power to significantly raise energy costs.

While there have been some changes to the Companies' fleets since 2005, according to the IMM, the Companies remain able to exercise considerable market power and would be “pivotal suppliers” in the relevant constrained markets—e.g. generators from whom the State or FRR Entity would have no choice but to purchase capacity in an FRR regime. It is therefore noteworthy that the Companies' comments blithely dismiss the potential for market power concerns in a single, brief paragraph. The paragraph asserts that any such concerns would be addressed through competition among the clean resources and price caps if procurements are undersubscribed. (Companies' Comments at 17).

While this may sound good in theory, it is undeniable that the Companies currently own, and will continue to own, the vast majority of clean (and fossil) generation located in New Jersey,

Pennsylvania and Maryland, a portfolio that PSEG appears poised to further expand by adding offshore wind facilities. Further, up to 7000MW of the Companies' generation in neighboring states could potentially be imported into New Jersey through existing transmission facilities. Given the narrow local delivery areas that are the focus of FRR, there can be little question that the Companies will at all times own a dominant share of the available capacity resources and will remain pivotal suppliers with whom FRR Entities and the State will be compelled to deal.

While the Companies would have the Board ignore market power or affiliate abuse concerns, literally every comment provided by stakeholders, including most notably the IMM, articulated significant concerns regarding the combined Companies' market power. The market power concerns are amplified in an FRR context, which would impose additional limitations on the scope of "competition" while removing the protective devices associated with the more expansive and competitive PJM RPM auctions. These factors are addressed at length in NJLEUC's Initial Comments.

In sum, despite the Companies' suggestions to the contrary, market power—the ability to inflate costs above competitive levels—remains a serious concern that would be amplified by the adoption of an FRR regime. The market power concerns are real and they doomed the PSEG/Exelon merger years ago. Market power remains a significant concern that in and of itself would provide a sufficient basis to justify rejection of the Companies' proposed Integrated FRR Procurement Methodology (without consideration of the many other reasons that would provide a basis for denial of the Companies' proposal).

In sum, Companies having the combined generation fleets and market power of PSEG and Exelon should not be given an opportunity to operate in an FRR environment in which the markets are constrained and limited in scope, have few rules or consumer protections, where the Board's

authority would be unclear absent significant amendments to EDECA, and where the potential for unintended consequences, particularly with regard to the BGS auction and competitive marketplace, is high.

B). JCP&L: The (Unwilling) FRR Entity?

In an obvious attempt to deflect concerns regarding the Companies' extraordinary market power within the relevant markets, the Companies suggest a phased approach to FRR in which one of the EDCs would be selected as the State's initial FRR Entity, responsible for all aspects of the Tier I procurement of capacity and environmental attributes. The Companies suggest, without actually so stating, that the EDC would not be PSE&G or Atlantic City Electric. As described by the Companies: "The Board could select a zone large enough to procure capacity from the clean resources currently supported by the State, as well as to accommodate a significant increase in new renewable resources (both solar and offshore wind) that will effectively be excluded from the PJM capacity auction as a result of State support. Ideally, the selected zone would not have locational constraints requiring the use of in-zone resources..." (Companies Comments at 4).

The Companies' Comments would require the FRR Entity to be responsible for, among other things, conducting a complicated procurement process in which it selects pre-determined quantities of capacity from renewable and clean energy resources, together with any necessary residual procurements, determines procurement winners, and negotiates long-term contracts for bundled capacity and environmental attributes for an agreed all-in price. According to the Companies' proposal, an EDC that follows the proposed procurement process "would be deemed to have acted prudently and would be guaranteed to recover its costs" through a "Clean Capacity Charge" assessed on all retail customers in the State. The EDC would also be permitted to

securitize its cost recovery, assuming appropriate enabling legislation is approved. (Companies' Comments at 8-10). The FRR Entity would also be responsible for paying the selected generators the sum of the capacity charge imposed on retail customers within its zone and the environmental attributes charge imposed on all retail customers throughout the State and collected through the EDCs' bills.

It is evident that the Companies' proposal would impose significant responsibilities and risks on the EDC selected to be the initial FRR Entity. It should also be recognized that regardless of which EDC is involved, the EDCs (as well as the Board) have been out of the business of resource planning and generation procurement since 1999 when the industry was restructured and generation became a competitive service. Therefore it is likely fair to state that none of the EDCs, including PSE&G, currently have the personnel, expertise or resources in place to competently perform the role of FRR Entity, a role that up to now has only been assumed by vertically integrated monopolies like AEP, Duke and Dominion that operate in regulated states and are quite accustomed to performing, among other functions, resource planning and load projections.

It is also evident that the zone described by the Companies is the JCP&L service territory. Of the various scenarios modeled by the IMM, the JCP&L zone is the largest and, as contrasted with the highly concentrated PSEG and NJ FRR zones, is considered "moderately" concentrated for market power purposes. (IMM Report at 10). The JCP&L zone is less concentrated than the other zones because, unlike PSEG, JCP&L divested its generation fleet as part of the restructuring and currently owns only a 321 MW hydroelectric power plant. The IMM notes that the JCP&L zone has a shortfall in capacity and would therefore have to acquire capacity from other New Jersey resources to satisfy the load requirements for its zone. Nevertheless, the IMM found that the JCP&L zone failed the more indicative and critical "pivotal supplier" test of market power,

meaning that even in the JCP&L zone, JCP&L, as FRR Entity, would have no choice other than to negotiate bilateral purchase agreements with the Companies, whose capacity would have to be procured to satisfy the Tier I load requirements and FRR rules. (IMM Report at 6, 10-11, 33).

So what do JCP&L's comments say about JCP&L's appetite to undertake these considerable responsibilities and the company's views of FRR generally? Ironically, JCP&L falls far short of offering a full-throated endorsement of the FRR alternative. Nor does JCP&L volunteer to be the FRR Entity, the implementation arm of the Companies' proposal. Rather, JCP&L's comments encourage the Board to adopt a "measured" approach in considering "alternatives for the State's energy future". Consistent with this measured approach, JP&L urges the Board to "ensure that the chosen course of action does not give rise to unforeseen risks and additional costs for utility customers" and to "carefully consider the potential impacts and attempt to mitigate the risks that this fundamental change may impose on the EDCs and New Jersey' customers". JCP&L also expresses satisfaction with the ability of the BGS auction to produce reasonable, market-based prices.

While JCP&L states that it is "possible" for the EDCs to develop an FRR approach, JCP&L seeks assurances from the Board that, if FRR is adopted EDCs will (i) be allowed to timely recover their reasonable and prudent costs to provide (BGS) service, including recovery of FRR non-performance penalties and (ii) be held harmless from FRR-related performance and other risks. (JCP&L Comments p.1-3). It is fair to state that JCP&L's comments express more concerns with, than confidence in the FRR alternative and clearly cannot be read as JCP&L's agreement to assume the significant obligations and potential risks associated with being the FRR Entity.

It is noteworthy that similar comments were proffered by Rockland Electric, which indicated its support for market mechanisms and solutions that promote competition and lower

consumer costs. With regard to the FRR alternative, RECO stated: “The shift to a construct that may require executing longer term contracts than entered into in the PJM capacity market and/or increase market power for certain generators could result in: (1) higher costs to customers than would otherwise be paid by securing capacity through a market construct; and (2) an inappropriate shift of generator investment risk from developers to customers. Seeking to avoid these outcomes, the Company continues to support efforts to explore market-oriented solutions, such as carbon pricing, to improve market operations and support the development of clean energy resources.” (RECO Comments at 1). RECO therefore recommends that the Board conduct a thorough analysis of the options available to support clean energy development in the State.

It is also interesting to note that the Comments of Atlantic City Electric were limited to responses posed by the Board regarding the BGS auction, and indicated that the FRR approach could support the BGS auction as currently structured: “*At this writing*, the Company supports the FRR approach to procure clean capacity within the existing framework of the current BGS construct.” (ACE Comment, p. 3) (emphasis supplied). ACE’s seemingly “hedged” comments were otherwise silent regarding the merits of the FRR approach, the Companies’ proposal or ACE’s willingness to assume the role of FRR Entity.

As noted in our Initial Comments, and in light of the tepid support for FRR generally by the EDCs other than PSE&G, significant threshold questions are posed, including (i) whether the Board has the authority to compel a reluctant EDC to become an FRR Entity in its delivery zone and assume all of the responsibilities and risks associated with the role (the Companies acknowledge that legislation would be required to enable the Board to select an EDC) and, if so, (ii) whether it is appropriate to shift to ratepayers responsibility for an FRR Entity’s mal-

performance or non-performance of its various FRR obligations, including responsibility for the crippling performance-related penalties that could be assessed by PJM.

C). Establishing The Cost Of Capacity And Environmental Attributes

Under the FRR paradigm established by the PJM tariff, the cost of capacity would be established through bilateral negotiations between an FRR Entity and eligible generators located within the FRR Entity's local delivery area and, as needed, in the larger EMAAC and MAAC zones. In our initial comments, NJLEUC argued that this approach is problematic because the FRR alternative removes the procurement of capacity from the PJM RPM auction which, despite its faults, is a workably competitive structure in which a multiplicity of diverse generators offer capacity in accordance with rules intended to protect consumers, including oversight by the PJM Independent Market Monitor. Our comments noted that in states like Ohio and Virginia, which are among the few regulated states that have adopted the FRR alternative, FRR Entities have been paid rates for capacity that significantly exceed the prices established in the PJM base residual auctions. Indeed, the desire to continue to earn above-market capacity rates was the reason why utilities like AEP helped create the FRR alternative in the first place, to preserve the capacity prices they had been earning as vertically integrated utilities in regulated markets under a cost of service regime.

Here, however, not content with the windfall profits that would be available to them under the FRR alternative, the Companies have produced an uninvited and expansive proposal for an "Integrated FRR Procurement" that would bundle, in a single procurement, both capacity and the "environmental attributes" associated with clean energy resources, purportedly to "standardize" the State's support for clean energy and encourage competition among the different clean energy

technologies. Under the Companies' proposal, offshore wind, solar and nuclear facilities would compete to sell their bundled capacity and environmental attributes for an "all-in price" fixed at the outset of a long-term contract, and offset by forecasted energy and ancillary services revenues. The Board would "oversee" the procurement process and the State would establish a limit on the all-in price ratepayers would pay for the bundled products. Any needed residual capacity would be procured for one year terms. If clean resources fail to economically satisfy the full requirements of FRR, gas resources would be procured to provide the balance needed. (Companies' Comments at 3).

The Companies argue, without further explanation, that their proposed approach would allow the State to achieve the EMP goals "at a lower cost than they would otherwise pay by avoiding the inefficiencies that will result from FERC's new bidding rules in the PJM capacity auction." Apparently this would be achieved through a requirement that customers pay the same capacity charge they would have paid if their EDC had not become an FRR entity [i.e. the same supposedly MOPR-distorted capacity price that we thought we were "escaping" through the FRR alternative]. The balance of the bundled charge would be treated, as with ZECs, as payment for the resources' environmental attributes. Therefore, if their proposal is adopted, the Companies state they would abandon the ZEC program. (Companies' Comments at 3-4).

So if the PJM's competition-driven, MOPR-distorted capacity market produces lower prices than forecast when setting the cap or actual floor price for the five-year, all-in priced FRR contract, the clean energy generators would get to pocket the difference. This affords the generators the ability to advance the illusion that ratepayers would get the upside of PJM competitive markets without actually having to participate while simultaneously "uncapping" the ZEC price, which would now equal the all-in price minus the PJM capacity price. The Board should not be fooled

by this regulatory three card Monty, ratepayers will pay the all-in price, which likely will exceed the current aggregate of PJM capacity plus ZEC charges.

However, it is the Companies' willingness to so readily abandon the \$300 million per year they receive under the ZEC program that raises a red flag and suggests what their proposal would be worth to the Companies and their shareholders, to whom, we are repeatedly reminded, they owe a fiduciary duty. These are, of course, the same shareholders whose interests PSEG purported to advance when it threatened to close all three nuclear plants unless all were awarded ZECs (notwithstanding the provisions of the ZEC Law that required each plant to be separately reviewed and approved on its own merit). We leave it to the experts to quantify what the Companies' exercise of market power under their proposal could mean in real dollars. For our purposes, suffice it to say that any suggestion that the Companies' abandonment of the ZEC program will somehow result in ratepayer savings should be readily dismissed as wishful thinking.

In addition to the likelihood that the Companies' proposal will result in significant and unwarranted financial windfalls to the Companies, the proposal would also create a new regulatory paradigm that would, among other things, partially re-regulate the Companies' nuclear plants and other generation facilities and shift the risks associated with their operation to ratepayers—a lose/lose scenario for ratepayers, representing a wholly unjustified and asymmetric remedy for the “ill” the Companies propose to remedy.

So what is behind the Companies' “generous” offer to help the State accomplish its EMP goals and escape Federal regulation that threatens those goals? As we unfurl the Companies' flag a bit to peek behind the curtain, the answer becomes clear. It is evident that the Companies seek to institutionalize and expand the unjust and unreasonable ZEC “environmental attributes”

subsidy, which has become the latest source of windfall profits to benefit the nuclear plants since stranded costs were awarded as part of the deregulation of the electric industry in 1999.

At the time, PSEG convinced the Board and State that its generation fleet would lose money in the newly-competitive generation markets and that a \$3 billion bailout was needed to offset the projected losses. However, PSEG Power, and in particular the nuclear plants, did not lose money and, in fact, soon became the cash cow that powered the profits of the Public Service Enterprise Group for many years. Thus, the stranded costs, which EDECA made irrevocable, merely served to provide an unneeded fifteen year financial windfall for PSEG. This is a mistake that cannot be repeated. In fact, any serious discussion of potentially *re-regulating* the nuclear plants as the Companies propose--the “poison label” on the bottle that Alice insisted on reviewing before she drank--should begin with PSEG’s agreement to return the \$3 billion it should never have received.

How would this partial re-regulation of the nuclear plants occur? The Companies’ proposal speaks in general and benign terms about empowering the Board to “oversee” the procurement of capacity and environmental attributes and to set “limits” on the all-in price that ratepayers would pay for these products. How the Board would be empowered to oversee the procurement of capacity on a statewide basis and determine the limits of ratepayer exposure is not explained, although the Companies acknowledge that the proposed arrangement is not lawful under EDECA and that new legislation would be required.

For once we agree. EDECA made competitive the utilities’ generation function and eliminated the Board’s authority to regulate generation-related rates and to engage in integrated resource planning for generation facilities. Under EDECA, the price of generation and decisions to develop or retire power plants are determined by the competitive markets and the price signals they provide to power plant developers. In short, EDECA shifted generation risk “off book”, away

from the State's regulated utilities and their ratepayers and onto unregulated generation providers, an allocation of risk that the Companies' proposal would now reverse.

Given this, it should be readily apparent that the Companies' proposal would totally upend this two decades-long regulatory paradigm. However, it should be clear that the proposal would not return us to the status quo that existed prior to 1999. Rather, the proposal would impose a structure in which ratepayers would pay regulated rates for the nuclear plants' capacity and environmental attributes, and assume the risks associated with the resource planning and performance of the plants' generation capacity under an FRR regime, and likely the plants' operational and business risks, as occurred with ZECs.

Further, there is no question that the Board has been out of the generation resource planning and generation ratemaking business since EDECA was enacted. Therefore, the Board currently lacks the internal resources and know-how needed to "oversee" procurements of capacity. This is the role that PJM currently plays through a sophisticated complex of rules, agreements and procedures, as well as active oversight by the highly competent Independent Market Monitor. If the Board's goal is to protect the interests of ratepayers in the pricing of capacity and environmental attributes and to provide meaningful oversight of the procurements, it would need to replicate PJM's complicated thicket of regulation and retain an adequate staff and roster of outside experts to fulfill these new obligations. Clearly, the proposal would not place the Board in an analogous role to the one it plays in overseeing the BGS auction, as BGS is a regulated default service and not a competitive product. Nor could the Board simply rely on an auction manager to conduct an auction and ratify its results. Much more is at stake, not the least of which would be the FRR requirement that capacity resources be accurately projected and fully available eight years into the future or risk the imposition of draconian financial penalties.

And how would the “all-in price” be established? The Companies’ proposal is curiously silent in that regard. Recent history, however, strongly suggests that the Companies would advocate a “method” similar to the one used in setting the initial ZEC rate. Senator Bob Smith was quoted as saying that the \$0.004/kWh value included in the ZEC Law for the “environmental attributes” of the nuclear plants was given to him by Ralph Izzo. No formal hearing was conducted to determine whether the figure accurately valued the plants’ environmental attributes or represented a just and reasonable rate, and the matter was remanded to the Board for final determination. The record later developed before the Board--which included a detailed analysis by the Board’s own outside consultant--demonstrated that the amount provided by Mr. Izzo was not only overstated, but wholly unwarranted. Nonetheless, the Board reluctantly concluded that its hands were tied under the language of the ZEC Law, which the Board interpreted to preclude it from revisiting the amount of the subsidy until after the first three year delivery period had expired. The Board Order is now on appeal, and the primary issues before the Appellate Division are whether the arbitrarily determined ZEC rate is just and reasonable and whether the due process rights of stakeholders were violated in the administrative proceeding.

Is the past a prologue to the future? It would surprise no one if the Companies were to again seek to characterize as “highly confidential” all of the financial information needed to determine an appropriate “all-in price” for capacity and the environmental attributes, to be shared only with Board staff and Rate Counsel. This would again relegate to the sidelines ratepayer intervenors like NJLEUC, which has consistently been permitted to intervene in countless proceedings, including the PSEG/Exelon merger proceeding, in which it has been afforded full access to similar financial information regarding the Companies.

An issue as critical as the pricing of the capacity and environmental attributes, separately or as a bundled rate, should not be determined behind closed doors, on an invitation-only basis, with so-called “non-essential” parties denied a meaningful role in the process, or based on evidence not included in a public record. This Star Chamber-like approach was never utilized in the past to determine generation-related rates for the utilities when they were regulated as vertically integrated monopolies and it is not a defensible substitute for a rate case. To institutionalize such an approach would represent a tremendous step backwards and would undermine the Board’s statutory obligation to establish just and reasonable rates through contested proceedings conducted in accordance with the Administrative Procedures Act. N.J.S.A. 48:2-21.

Moreover, by setting all-in price ceilings and establishing carve-outs for various resources, the Board would essentially place itself in the position of picking winners and losers in a re-regulated environment. Adopting the Companies’ proposal would sacrifice the competitive market efficiencies and consumer protection devices offered by the PJM auctions and substitute what easily could develop into a formula rates-type substitute, a rate setting device long sought by PSEG but historically rejected as unpalatable, particularly given the effect formula rates have had on transmission rates at FERC.

Ironically, the Companies suggest that they have no idea what rate impacts their proposal would produce because the issues are “complex and demand considerably more study”. The Companies acknowledge that the “ultimate environmental benefits are enormous, but they will necessarily require increases in customer electric rates”. (Companies’ Comments at 12). However, the fact that the Companies would so readily give up \$300 million annually in ZEC payments clearly suggests that they have a very good idea what the rate impacts would be and that they, too, would be enormous.

D). What Capacity Resources Would Be Included In The Tier I Procurement?

Under the Companies' proposed Tier One procurement, the FRR Entity would attempt to fill as much of its capacity plan as possible with State-supported clean energy resources targeted by FERC's MOPR. These resources would "compete" for long-term contracts to sell bundled capacity and environmental attributes to the FRR Entity at an all-in price set at the beginning of the contract term. The resources would be selected in the following order "to achieve the technology specific goals of the EMP, while at the same time harnessing competition to reduce prices for offshore wind and new solar": first, a carve-out for offshore wind and solar, with the remaining quantity needed for the FRR zone from either offshore wind, grid-connected solar or the nuclear units selected to receive ZECs. To the extent that the Tier I procurement does not procure sufficient capacity to satisfy the FRR zone requirements, a residual procurement for one year contracts would be conducted and include other clean energy resources within EMAAC and MAAC to the extent possible given transmission constraints. If necessary, gas fired resources could be included to round out a procurement. (Companies' Comments at 8-9).

While the proposal may have superficial appeal to some, an analysis of the load requirements and the clean energy resources currently and projected to be timely available to meet those requirements in New Jersey and the larger EMAAC and MAAC zones reveals that the procurements would be completely dominated by generation owned by PSEG and Exelon Generation. Thus, for example, if we continue to assume that JCP&L would be selected as the initial FRR Entity, the IMM report indicates that JCP&L has a zonal unforced capacity obligation of approximately 6,500MW, with a statewide total of about 20,000MW. After taking into account the add-back associated with energy efficiency initiatives, the IMM calculates a 2,448 MW UCAP

or 39% FRR shortfall based on the resources currently located within the JCP&L zone. (IMM Report at 12 and 14).

The IMM Report indicates that the installed clean energy capacity currently located within the JCP&L zone is limited to only 58 MW of solar (unspecified as to type) and 321 MW of hydroelectric power, and a combined total of about 300MW of demand response and energy efficiency. (IMM Report, Table 3 at 8). There is no offshore wind in the zone, which is dominated by about 3000 MW of natural gas-powered generation. (We note the pattern of installed capacity by fuel source is similar in the AECO zone, should ACE be viewed as the initial FRR Entity instead of JCP&L.) The IMM Report notes that in the 2018-2019 compliance year, New Jersey had to import 97.7 percent of the total RECs that met class I RPS standards. (IMM Report at 9). Thus, the wind and solar resources located within the JCP&L zone and elsewhere in the State that satisfy the requirements for the Tier I procurement represent only a small fraction of the total unforced capacity needed to serve the JCP&L zone.

Nor are other major new renewable energy projects coming online until 2024 at the earliest, when the Orsted 1100 MW tranche of offshore wind is scheduled to achieve commercial operation. The second 1100 MW tranche of offshore wind is not expected to achieve commercial operation until 2027 at the earliest. It is important to underscore that even if all of the 7500 MW offshore wind goal is achieved, these combined resources would still fall far short of satisfying the JCP&L zone's unforced capacity requirements. This is so because the 1100 MW associated with each tranche represents only the nameplate capacity of the offshore wind resources. Because they are only intermittent resources, the actual unforced capacity value that PJM would attribute to each 1100 MW facility would be reduced to 26 percent of the nameplate capacity, which means that only 286 MW of capacity would be attributed to the Ocean Wind project, as well as all subsequent

tranches. We also note that PSEG's apparent intention to enter the offshore wind market will only further increase PSEG's share of the capacity eligible for the Tier One procurement.

It is therefore clear that in the near and long term, the Companies' Salem I and II and Hope Creek nuclear facilities, which have a combined total of about 3500 MW of unforced capacity, would represent the overwhelming majority of "clean energy" resources available to satisfy the Tier I procurement under the terms proposed by the Companies. (IMM Report, Table 3 at 8). Given the shortfall in clean energy resources available within the JCP&L (or AECO) zone, to the extent that there is import capability into the JCP&L zone—generally assumed to be up to 7000 MW-- the procurement would then extend to clean energy resources located within the larger EMAAC zone. These resources include the Limerick (Exelon) and Peach Bottom (PSEG/Exelon) nuclear stations in Eastern Pennsylvania and Exelon's Calvert Cliffs nuclear station in Maryland.

It should be obvious to all that the Companies' generation dominance over the JCP&L and other delivery zones in New Jersey, similar to the concentration level that led to the denial of the PSEG/Exelon merger, would enable the Companies to exercise extraordinary market power. The notion that the Board would oversee the procurement process and purportedly be empowered to establish ceiling prices may provide some comfort by suggesting the appearance of Board control over the process. However, the appearance would likely be illusory.

Consider that an effective way to exercise market power has historically been through the monopolist's strategic withholding of a product from its relevant marketplace. Given this, what would occur if the Board were to exercise the "authority" granted it under the Companies' proposal and establishes an all-in ceiling price for the bundled products that the Companies consider to be too low—e.g. the price values capacity at the PJM BRA rate and the environmental attributes at a value that is less than the current ZEC subsidy? If the Companies decide not to bid their products

because the ceiling price would not afford them the return needed to satisfy the fiduciary obligation owed to their shareholders, what would the Board do then? If one considers this scenario to be unlikely to occur, we need only recall PSEG's threat to close its nuclear plants if all were not awarded ZECs, a move that could have compromised the reliability of the State's electric grid. One high stakes game of chicken is one too many. The State should not knowingly put itself in the position of weakness that would clearly result from the Companies' proposal.

E). A Cost/Cost Analysis Of FRR And The Companies' Proposal

Ironically, most of the comments provided by solar and offshore wind companies—purportedly the “beneficiaries” of the Companies' proposal—were quite vocal in their opposition to the FRR alternative. Many of these companies agree that the potential benefits from FRR are particularly slim in comparison to the potential for significant increases in costs, exercises of market power, threats to competition and the BGS auction, ratepayer risk and the undesirability of the substantial changes that would occur to the decades-old regulatory paradigm. Thus, for example, the comments provided jointly by Advanced Energy Economy/American Wind Energy Association/Mid-Atlantic Renewable Energy Coalition and the Solar Energy Industries Association were typical and instructive:

“...If New Jersey is unable to procure a sufficient amount of capacity through an FRR procurement process, it will have to pay an insufficiency charge equal to double the Net Cost of New Entry, in the applicable delivery year for every MW of shortfall. Accordingly, the Board needs to carefully assess the balance between the risks of paying insufficiency charges associated with any capacity shortfalls under an FRR construct with the potential benefits of any FRR. In the near-term, there may well be more costs than benefits if FRR is implemented. In the next several years, New Jersey faces the risk of 300 MW UCAP of OSW not clearing. Not receiving capacity credit for those megawatts may pale in

comparison to increased costs of going FRR. (AEE Comments at 23) (emphasis supplied).

These comments are consistent with the analysis of multiple stakeholders, who have concluded that the only real problem posed by the MOPR for years to come is the threat that the first tranche of offshore wind will not clear the PJM auction. The 300 megawatt capacity cited as representing the amount of offshore wind capacity that is at risk is also consistent with the comments of a number of knowledgeable stakeholders, including the IMM. These stakeholders have concluded that the problem “cured” by FRR boils down to 286 MW of capacity associated with the Ocean Wind project, which most agree likely would not clear in the PJM auction. This reality provides the basis for these commenters’ conclusion that FRR “could lead to rate increases potentially far greater than those created from the exclusion of offshore wind from the capacity market”. See, Comments of Atlantic Shores Offshore Wind, LLC at 5; Comments of Environmental Defense Fund at 4; Joint Comments of New Jersey Conservation Foundation and New Jersey Sustainable Business Council at 1 (“The additional cost (the MOPR) exclusion would cause for New Jersey electricity consumers is relatively small and may, therefore, not warrant the risk and unknown costs of alternatives to the PJM capacity market”); and Advanced Energy Management Alliance at 4, to a similar effect.

While each expressed the thought differently, these commenters all agreed that the Board should proceed cautiously in considering the FRR alternative. Each urged the Board to weigh FRR’s minimal financial benefit against the vastly more significant risks associated with exercises of market power and changes to the regulatory paradigm under an FRR regime. It should be kept in mind that these comments were addressed only to FRR and the Board’s questions to stakeholders, and not to the Companies’ proposal which, we suggest, would likely only exacerbate the concerns expressed.

It is noteworthy that Orsted, the developer of the Ocean Wind project, agreed that the loss of capacity revenues associated with the project would not be significant: "...for Orsted's 1100 MW Ocean Wind Project approved by the Board, if the Project does not clear the auction, the loss of capacity revenues is estimated to be more than \$40 million of value annually for an approximate rate impact of 0.1% on New Jersey's electric rates". (Orsted Comments at 5). Of the commenters who did the calculation, Orsted's projected revenue loss figure is the highest. In contrast, the New Jersey Conservation Foundation and New Jersey Sustainable Business Council provided the following calculation:

"...the added cost caused by the MOPR must be included in evaluation the cost of the FRR versus that of the status quo BRA/MOPR alternative. The likely impact of the MOPR in the first several BRAs...would likely be to prevent the bids of the 1100 MW of offshore wind New Jersey has already contracted for, from clearing in the BRA auction. This would, in turn, require New Jersey LSEs to purchase an extra 286 MW of unforced capacity in the BRA, which would cost \$18.2 million per year, if purchased through the BRA at current price levels, allocated pro-rata across New Jersey's zones." (Comments at 4) (emphasis supplied).

The calculation was confirmed by others, including the New Jersey Conservation Foundation and Sustainable Business Council (Comments at 4) and the Calpine Corporation, which confirmed the 286 MW capacity figure but derived a slightly different cost figure assuming a BRA price of \$186.16/MW-day figure to derive a figure of \$19.4 million of RPM capacity revenues per year. Calpine noted that this revenue figure is "less than the potential increase in costs that New Jersey ratepayers could see from using the FRR alternative" and would be consistent with the 1200 MW of offshore wind capacity to be solicited this year for operation in 2027. (Calpine Comments at 5).

Calpine's observation that this lost capacity revenue figure, as independently verified by these stakeholders, is less than the potential increase in costs that could result from adoption of the

FRR alternative is clearly an exercise in understatement. NJLEUC noted in our initial comments that the PJM Independent Market Monitor had determined that the cost of capacity for New Jersey could increase by up to \$386,448,104, or 29.6 percent higher than the 2021/2022 BRA, using the BRA clearing price as the baseline. The IMM's figure specifically did not take into account the multiplier effect that could result from an unchecked exercise of the market power that the Companies have consistently been found to wield in the PSEG and EMAAC zones. The IMM observed:

Based on this analysis, the creation of a New Jersey FRR, a PSEG FRR or a JCPL FRR is likely to increase payments for capacity by customers in New Jersey. It is expected that the actual price for capacity in New Jersey would be the result of a negotiation between the owners of the required capacity and the State of New Jersey. The price for capacity resources could substantially exceed the capacity market clearing price and the capacity market offer cap. (IMM Report at 4).

The potentially significant increase in costs imposed upon unsuspecting New Jersey ratepayers by the FRR alternative is further revealed through analysis of the capacity rates imposed in the few regulated states that have implemented FRR. As noted in the Comments filed by the Electric Power Supply Association, “in the limited circumstances where FRR has been utilized, customers in FRR areas in Virginia have paid up to 4 times more than the rest of the customers in the PJM region for capacity with no additional benefit than that procured by RPM”. EPSCA noted that similar to New Jersey, in Virginia, Dominion Energy filed an Integrated Resource Plan to comply with analogous Virginia laws that require 100% clean energy by 2050. Dominion's plan was designed to expand renewables to comply with the state's clean energy mandates, but the price tag was significant—“the second to least aggressive option includes a \$45.92 increase *per month* on customer electric bills by 2035”. (EPSCA Comments at 6) (emphasis supplied).

In the same vein, the PJM Power Providers Group noted that the FRR rate paid by ratepayers in Virginia's Appalachian Power Company's service territory was \$403.35/MW-day. During the same period, New Jersey ratepayers paid a rate of \$119.77/MW-day. If New Jersey ratepayers paid at the same rate as Appalachian Power's customers, they "would have paid a staggering \$2 billion more this year". (Comments of PJM Power Providers Group at 10) (emphasis supplied).

As noted in NJLEUC's initial comments, the first utility to adopt FRR was Ohio-based American Electric Power Company. According to the IMM, AEP, a vertically integrated utility operating in a regulated state, opted out of the PJM capacity market to enable it to continue to receive payment for capacity "well in excess of capacity market prices, based on a cost of service model, under a regulatory arrangement with Ohio". (IMM Report at 5). According to Calpine Retail, the FRR framework "harmed the competitive market in Ohio and resulted in higher rates to customers." Competitive suppliers in Ohio must pay an artificially high capacity charge to AEP and have effectively been priced out of the market because the above-market capacity charges more than offset the savings that retail suppliers can offer customers. (Calpine Retail at 5).

The IMM's comments in this proceeding effectively make this point in more general terms:

"...It has been demonstrated repeatedly in New Jersey and elsewhere that long term, guaranteed contracts are generally not a good method for purchasing power, regardless of its characteristics, in a cost effective manner. Reliance on markets, subject to oversight, regulation and good market design, is preferable to relying on FRR type constructs which are nonmarket, planned approaches that rely on the judgment of planners rather than on providing incentives to market participants and shifting risk from customers to market participants. To the extent the FRR constructs provide incentives to planners to enter into long term contracts, the FRR approach will shift risks from investors to customers, which is an inefficient and ineffective and costly design". (IMM Comments at 4).

Thus, apart from the rate increases that appear inevitable under FRR—increases that would occur at a terrible time for struggling ratepayers in this COVID environment—the significant risks inherent in the regulatory paradigm shift urged by the PSEG and ExGen should give the State considerable pause. The IMM’s observations regarding FRR focused on a critical risk element that would increase exponentially under the Companies’ proposal—the shifting of operational risk of the generating units from shareholders to ratepayers, as well as the risks associated with the draconian FRR performance penalties.

NJLEUC addressed several of these risks in our initial comments and will not comment further here. For present purposes, however, suffice it to say that even when the EDCs were regulated as vertically integrated monopolies, ratepayers were not required to assume the EDCs’ operational risks. Therefore, to the extent that the Companies’ proposal would have ratepayers assume these risks—both for capacity and environmental attributes in the same manner as they are treated in the ZEC Law--the Companies propose a Frankenstein-type version of re-regulation that, as the IMM points out, would transfer these risks from shareholders, where they belong, to innocent ratepayers who would become the guarantors of the Companies’ nuclear plants.

Further, saddling ratepayers with responsibility for FRR performance penalties resulting from faulty resource planning or load projections would expose ratepayers to potentially breathtaking financial penalties. JCP&L’s comments made clear that JCP&L fully understands the scope of its potential exposure to crippling FRR penalties were it to become the FRR Entity. This explains why its comments included the demand that “the Board needs to make clear that the EDCs will receive timely recovery of any such penalties and/or costs, to the extent that such penalties and/or costs are not recovered directly from capacity resources”. (JCP&L Comments at 3).

Under JCPL&L's preferred scenario, the FRR Entity would be indemnified and ratepayers would be responsible if the FRR Entity or the Board in a resource planning investigation failed to accurately project the all-in load for the FRR zone up to eight years in advance. As we previously noted, if a projection was made last December for the State's load requirements this month, the projection would likely be off by 10% or more given the unanticipated COVID epidemic. What are the odds that an accurate projection could be made 8 years into the future? The only thing certain under FRR would be the significant penalties that would be imposed for an inaccurate projection. The Board need look no further than PSE&G's grossly inaccurate multi-year stranded cost projections during the restructuring process to grasp the potential magnitude of mistaken projections under FRR. The FRR's penalty element was intended to—and should—make the FRR alternative an unattractive choice. Given the huge financial risks it would impose on ratepayers, the Board should take the hint concerning FRR's unattractiveness and act accordingly.

The final "costs" of FRR and the Companies' proposal are those that would be borne by the Board and the State. As noted in our initial comments, the Board would have to resume generation resource planning and implement a system of oversight over capacity and environmental attributes procurements that replicates the complicated PJM approach, including active oversight by the State equivalent of an independent market monitor. The Board has not been involved in these functions since 1999 and adopting the Companies' proposal would require an enormous undertaking by the Board to rise to the challenges posed by this new paradigm. This role would clearly be distinguishable from the Board's largely passive role overseeing the BGS auction, involving the procurement of a non-competitive, default product provided to non-switching customers. Under the Companies' proposal, the Board would be required to play an active role in determining and projecting load requirements, establishing defensible ceiling values

for the competitive products, and ultimately picking winners and losers in the procurements. It is difficult to conceive that the Board would willingly undertake these significant responsibilities in these circumstances.

Is it really worth all of this to avoid having to pay an extra \$18 million a year for offshore wind capacity?

Conclusion

In sum, the benefits of FRR and the Companies' proposals are so insignificant, and the potential costs so extraordinary that we must again underscore that the "cure" proposed is far worse than the "illness". The Board should heed the nearly unanimous comments of the many stakeholders in this proceeding to proceed cautiously, recognize the huge potential costs and risks involved, and understand that at the end of the day, the MOPR will likely not impose costs of great significance to the State. As several commenters suggested, even these costs may be obviated through negotiation with PJM as it formulates its implementation of the MOPR. We must also recognize that the MOPR may not survive the current appeal or a change in administration in Washington.

The Board should follow the lead of wise Alice and proceed cautiously, carefully “reading the label” first, before indulging in a regulatory brew that has the clear potential to be toxic.

Respectfully submitted,

Steven S. Goldenberg
Giordano, Halleran & Ciesla, PC
125 Half Mile Road, Suite 300
Red Bank, New Jersey 07701
sgoldenberg@ghclaw.com

and

Paul F. Forshay
Eversheds-Sutherland (US) LLP
700 Sixth Street, NW, Suite 700
Washington, DC 20001
paulforshay@eversheds-sutherland.com

Attorneys for the New Jersey
Large Energy Users Coalition

Dated: June 24, 2020

Docs #4428247-v1