

**STATEMENT OF THE ELECTRIC POWER SUPPLY ASSOCIATION**

**NEW JERSEY GENERAL ASSEMBLY**

**S-3061: BPU STUDY OF ZERO EMISSIONS CREDITS**

**MARCH 20, 2017**

The Electric Power Supply Association (EPSA) appreciates this opportunity to comment on S-3061, which would direct the New Jersey Board of Public Utilities to study subsidies for nuclear power plants and report back to the Governor and Legislature. The subsidies would take the form of so-called “Zero Emissions Credits” (ZECs) of about \$500 million per year. EPSA commends the sponsors of the legislation for not rushing to judgment as ZECs are highly controversial. It is prudent to take a cautious approach and thoroughly study *all* the many ramifications instead of rushing into adopting such costly and unlawful subsidies. EPSA believes that a comprehensive and balanced study will reveal the many flaws in the ZEC approach of subsidizing PSEG’s nuclear assets on the backs of ratepayers, while also undermining competition.

For twenty years EPSA has been the national trade association representing leading independent power producers and marketers. EPSA members provide reliable and competitively priced electricity from environmentally responsible facilities using a diverse mix of fuels and technologies, including assets in New Jersey and throughout the PJM Interconnection. EPSA members have invested billions of dollars at their own risk without ratepayer subsidies. They did so in reliance on the voluntary decisions of New Jersey and other states to depend on market forces to provide reliable electric service to consumers at competitive prices.<sup>1</sup>

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<sup>1</sup> These comments represent the position of EPSA as an organization, but not necessarily the views of any member with respect to any issue.

New Jersey nuclear plants targeted for consumer-financed ZEC subsidies are profitable today and committed to remain in operation for several years, providing ample time to thoroughly consider these issues before making a costly mistake in haste, as New York and Illinois did last year. A balanced study will show New Jersey what consumers in New York and Illinois are belatedly discovering<sup>2</sup>: ZECs provide unjustified and costly subsidies to some resources at the expense of consumers and other power suppliers that are just as necessary to provide reliable and affordable electric service.

ZECs are being pushed by utility holding companies that own both market-based generation and cost-based retail distribution utilities to finance new corporate strategies to boost earnings by exiting competitive generation to focus on more assured earnings from their retail rate-regulated utilities. ZECs value the jobs, tax payments, environmental performance, operational characteristics and other attributes of only *some, but not all*, sources of power generation necessary for reliable electric service. What *is* unique about New Jersey is that, unlike in New York and Illinois, PSEG is *not* claiming imminent financial distress for its nuclear plants. Instead, they cite the *mere potential* for future losses as justification for subsidies that will only drive the retail rate paid by consumers much higher through rate surcharges to make the ZEC payments.<sup>3</sup>

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<sup>2</sup> For example, the New York General Assembly (House) recently added a moratorium to its budget bill to suspend implementation of the New York ZEC program through December 31, 2018, until state officials appear before the Legislature in person to explain the New York Public Service Commission's controversial decision to approve ZECs for certain upstate nuclear units paid by all New York consumers.

<sup>3</sup> As adopted in New York and Illinois, ZECs force consumers to pay a whopping 50-75 percent more than necessary for the same electricity. An example illustrates the point. At present, consumers generally pay \$25-30 per megawatt-hour (MWh) for electric energy whether nuclear or non-nuclear (transmission and distribution is additional). The ZECs would require them to pay an *additional* \$17 per MWh for nuclear covered ZECs. Power suppliers without ZECs receive \$25-30 per MWh, while consumers are forced to pay an additional \$17 per MWh to nuclear plants covered by ZECs. This means New Jersey consumers would be forced by act of the Legislature to pay a premium of 56-68 percent over and above current prices for the same nuclear power consumers use today.

PSEG only recently started claiming that its nuclear plants may not be recovering their cost of capital to justify future investments and could be cash flow negative by 2020. This is apparently based on a comparison with illiquid forward power prices that *may or may not* accurately measure future revenues from these plants. For starters, if revenues below cost of capital and need to fund future investments are the standards to trigger consumer subsidies, many *non-nuclear* power plants (including those of EPSC members) would also qualify for out-of-market subsidies. Where would subsidies end? How will policymakers explain to other businesses that a company with a monopoly utility franchise gets special relief, but the State will not intervene to help non-electricity companies recover *their* cost of capital and help fund *their* future investments?

This is not the first time that lawmakers have been asked to force consumers to pay for these power plants. Thus, it is imperative for any study to consider the history of electric restructuring in New Jersey. Under that restructuring, PSEG already received almost \$3 billion in stranded costs including for the nuclear plants for which they now seek *additional* customer support with ZECs. In addition, when wholesale prices were generally double today's levels in the 2000s, nuclear power plants were *highly* profitable. Only *now* when market prices are at historic lows for *all* wholesale suppliers are nuclear plant owners seeking consumer-backed subsidies *yet again*. In short, ZECs are a third bite at the apple amounting to duplicative recovery. Making it worse, New Jersey consumers would be subsidizing nuclear power generation sold out of state.

In addition, PSEG may have contributed to the lower wholesale prices that it now claims justify ZECs when it undertook transmission expansion projects and increased its generation capacity. The transmission expansion was very profitable but it had the

effect of bringing in lower-cost resources from outside New Jersey to compete with PSEG's nuclear and other in-state power plants. That is good for consumers and shows the benefit of being part of a competitive regional power system through PJM. However, ZECs essentially seek to recapture those consumer savings to make the company financially whole regardless of whether it contributed to making its nuclear plants less competitive. In sum, ZECs would *socialize costs and risks* across consumers while *privatizing profits* for nuclear owners. The effect is to transfer wealth from New Jersey consumers to shareholders, many of whom are out-of-state residents.

To be of any real value, any study of ZECs should consider *all* the many factors and impacts of ZECs with an open mind. Ms. Stephanie Brand, Director Division of Rate Counsel, has made several excellent recommendations to make sure that any study is balanced and examines *all* the far-reaching impacts to New Jersey's competitive retail and wholesale electricity markets. Based on EPSA's review of S-3016, we respectfully request that it be refined through amendments which we have distributed to the Committee based on the following principles:

1. Make it clear that the purpose and scope of the study is not just on "feasibility and benefits" of ZECs as originally drafted, but rather on a neutral, balanced and comprehensive study of the pros and cons of ZECs;
2. Make it clear the study should examine the financial costs of every recommendation, including the impact on retail electric rates;
3. Make it clear the study should examine all steps to achieve agreed upon carbon reduction goals and whether ZECs are the least cost and most effective means to reduce carbon emissions;

4. Make it clear the study should include the impact of ZECs on retail competition in New Jersey and on the PJM wholesale markets;
5. Make it clear the study should put ZECs in context by documenting the amounts already paid by consumers for nuclear power plants as “stranded costs”;
6. Make it clear the study should examine what happens if ZECs are to make the New Jersey nuclear plant assets more valuable in a sale to new owners (as FirstEnergy has admitted is the purpose of ZECs it seeks in Ohio); and
7. Make it clear that the BPU should consider all relevant factors in addition to those spelled out in more detail and should take public input on the study.

EPSA and many others, including the PJM Independent Market Monitor<sup>4</sup>, strongly oppose ZECs because such subsidies undermine the markets that competing power plants rely on for revenues. EPSA believes that all generators should compete on the same terms. To the extent market rules need reforms, stakeholders should work together on fuel-neutral improvements to how wholesale electricity is priced and procured in PJM. ZECs needlessly shift risks associated from investors to captive consumers. ZEC-eligible resources strongly favor them precisely because they want to force consumers to pay them above-market prices. However, such subsidies erode the wholesale markets which all other market participants that contribute to reliable electric service in New Jersey depend on for revenues and to make their investment decisions.

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<sup>4</sup> See, *State of the Market Report for PJM 2016 Volume 1: Introduction pages 1-2* (March 9, 2017) (“The issue of external subsidies emerged more fully in 2016. These subsidies are not directly part of the PJM market design but nonetheless threaten the foundations of the PJM capacity market as well as the competitiveness of the PJM markets overall” citing Illinois ZECs as an example.) (“Subsidies are contagious. Competition in the markets could be replaced by competition to receive subsidies. PJM markets have no protection against this emergent threat.”) (“Once the decision is made that market outcomes must be fundamentally modified, it will be virtually impossible to return to markets.”)

The North American power grid, including the PJM portion, is comprised of hundreds of power plants deploying a range of technologies and fuels with various operating characteristics. No region has separate power grids for nuclear, renewables, natural gas or any other fuel. While nuclear plants provide base load power, they are quite inflexible at a time when changes in technology, customer preferences and public policies demand a more flexible power supply system. ZECs selectively grant some resources preferential treatment at the risk of highly adverse long term consequences at a time of dynamic changes in how electricity is generated, sold and used. The full impacts of singling out any one fuel (such as nuclear) in a physically and financially interconnected system must be thoroughly understood before significant harm is done that would be difficult to reverse. The scope of any ZEC study should be this broad.

ZECs are not about the adequacy of generation to continue to provide reliable electric service. New Jersey wisely joined the PJM Interconnection to tap the considerable reliability and economic benefits of being part of a regional power system. PJM assures reliability through transmission planning and resource procurement. This includes a three-year forward auction to line up capacity commitments on a least-cost basis far in advance to meet projected peak needs plus a reserve safety margin. The May 2016 base auction for the 2019-2020 delivery year even exceeded that reserve margin, procuring a reserve margin of 22.4 percent, well above the 16.5 percent target. If any power plant can demonstrate to PJM that it is needed for reliability but not recovering its costs, PJM can provide a mechanism to keep it running. However, this is a cost-based contract for a length tailored to the circumstances, not the pre-set ZEC price for a fixed term regardless of the plant's economics or how long it is needed.

PJM wholesale markets are delivering reliable service at competitive prices, indeed historically low prices. This challenges the economics of *all* power suppliers, not just nuclear. PJM and the Federal Energy Regulatory Commission (FERC) are actively working on these issues (FERC has scheduled a two-day technical conference for May 1-2, 2017). EPSA is confident that a thorough ZEC study by the BPU will conclude that regional solutions are the best approach for consumers and suppliers.

Finally, ZECs run considerable risk of being found by a federal court to be preempted by the Federal Power Act based on the U.S. Supreme Court's unanimous decision in *Hughes v. Talen Energy Marketing* (2016).<sup>5</sup> As EPSA contends in federal lawsuits now pending in both New York and Illinois, ZEC schemes constitute illegal interference in the FERC-regulated wholesale markets per *Hughes*. At a minimum, any ZEC study should examine these legal issues.

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<sup>5</sup> In a unanimous opinion, the Court struck down a Maryland scheme that, like ZEC schemes, require a State's electric distribution companies to enter out-of-market arrangements backed by customer surcharges with payments going to defined "special" resources. There in Maryland, as here with ZECs, the receiving power plant claimed that market revenues were insufficient and sought out-of-market payments based on "attributes" not being fully valued in the marketplace.