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August 31, 2016

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Hon. Kathleen H. Burgess
Secretary to the Commission
New York State Public Service Commission
Agency Building 3
Albany, New York 12223-1350

Re: Case 15-E-0302 – Proceeding on Motion of the Commission to Implement a Large-Scale Renewable Program and a Clean Energy Standard

Case 16-E-0270 – Petition of Constellation Energy Nuclear Group LLC; R.E. Ginna Nuclear Power Plant, LLC; and Nine Mile Point Nuclear Station, LLC to Initiate a Proceeding to Establish the Facility Costs for the R.E. Ginna and Nine Mile Point Nuclear Power Plants

Dear Secretary Burgess:

Enclosed for filing on behalf of Castleton Commodities International LLC and its affiliates, Roseton Generating LLC and CCI Rensselaer LLC, is an Application for Rehearing of the Commission's *Order Adopting a Clean Energy Standard*, issued on August 1, 2016 in the above-referenced cases.

Respectfully submitted,

THE DAX LAW FIRM, P.C.

John W. Dax

JWD:lmd
Enclosure
cc (via email): NY PSC Active Parties

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of:	:	
Proceeding on Motion of the Commission to Implement a Large-Scale Renewable Program and a Clean Energy Standard.	:	Case 15-E-0302
Petition of Constellation Energy Nuclear Group LLC; R.E. Ginna Nuclear Power Plant, LLC; and Nine Mile Point Nuclear Station, LLC to Initiate a Proceeding to Establish the Facility Costs for the R.E. Ginna and Nine Mile Point Nuclear Power Plants.	:	Case 16-E-0270

APPLICATION FOR REHEARING OF
CASTLETON COMMODITIES INTERNATIONAL LLC

Dated: August 31, 2016

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TABLE OF CONTENTS

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In the Matter of:	:	
Proceeding on Motion of the Commission to Implement a Large-Scale Renewable Program and a Clean Energy Standard.	:	Case 15-E-0302
Petition of Constellation Energy Nuclear Group LLC; R.E. Ginna Nuclear Power Plant, LLC; and Nine Mile Point Nuclear Station, LLC to Initiate a Proceeding to Establish the Facility Costs for the R.E. Ginna and Nine Mile Point Nuclear Power Plants.	:	Case 16-E-0270

APPLICATION FOR REHEARING OF
CASTLETON COMMODITIES INTERNATIONAL LLC

INTRODUCTION

In the *Order Adopting a Clean Energy Standard*, August 1, 2016 (*August 1 Order*), the Public Service Commission (Commission) adopted a Zero-Emissions Credits program (ZEC Program) that requires load-serving entities (LSE) to enter into contracts requiring them to purchase Zero-Emissions Credits (ZECs) from the New York State Energy Research and Development Authority (NYSERDA), and reimburse the NYSERDA for the costs it incurs in purchasing ZECs from the owners of four upstate nuclear-powered electric generators. The cost of the ZECs collectively is estimated to be nearly one billion dollars in the first two years of the ZEC Program (*August 1 Order* at 126), to be paid by New York's LSE's, and in turn their ratepayers, over and above what would be paid for electricity produced and sold in the competitive wholesale and retail markets. The price of the ZECs is derived by the Commission

from an estimate made by a federal government interagency task force of the social cost of carbon emissions (Social Cost of Carbon) converted to a per megawatt hour basis. The quantity of ZECs to be purchased will be based on the eligible nuclear plants' historic annual production of electricity.

Castleton Commodities International LLC (CCI), on its own behalf and on behalf of its affiliates, Roseton Generating LLC and CCI Rensselaer LLC, applies, pursuant to Public Service Law § 22 and 16 NYCRR § 3.7, for rehearing of the *August 1 Order* insofar as the *August 1 Order* adopted the ZEC Program. CCI seeks rehearing because its participation in New York's wholesale markets will be adversely affected by the ZEC Program, and because in adopting the ZEC Program, the Commission has acted beyond the scope of its legislatively delegated authority, has acted in an area pre-empted by federal law, has imposed an unlawful burden on interstate commerce and has failed to provide reasoned explanations for discriminating among sources of generation with reduced carbon attributes, for abandoning its commitment to competitive forces to manage the wholesale markets, and for how the Commission will administer the mixed reliance on competition and command and control regulation in the wholesale markets.

THE APPLICANT

CCI, through its affiliates and subsidiaries, generates and sells electricity at wholesale in both capacity and energy markets, including markets administered by the New York Independent System Operator (NYISO) as well as in neighboring Control Areas. As an active participant in wholesale markets subject to federal regulation and supervision, CCI and its affiliates have an interest in the proper functioning of those markets. The CCI entities are parties to this proceeding. Roseton Generating LLC and CCI Rensselaer LLC together with others

(collectively, the Indicated Suppliers) filed comments in opposition to the ZEC Program on July 22, 2016.

THE ZEC PROGRAM

As described in Appendix E to the *August 1 Order,* the ZEC Program consists of long-term contracts between NYSERDA and the upstate nuclear plant owners under which the owners sell the zero-emission attributes, expressed in $/MWh, associated with the specific volumes of electricity produced by their assets. Those contracts will be mirrored by mandatory contracts between LSE's and NYSERDA under which each LSE will purchase ZECs in an amount equal to its proportion of statewide load. ZEC's will be priced by subtracting from the Social Cost of Carbon, the payments made for Regional Greenhouse Gas Initiative (RGGI) allowances embedded in the market price of a MWh produced and sold in New York State, and, following 2018, an amount equal to the excess of the sum of (i) the forecast Zone A energy price and (ii) the forecast rest-of-state capacity price over $39/MWh. The production of ZECs will be enforced by a performance measure to be implemented by NYSERDA such that if the production falls below 85% of the historic production levels, the obligation to purchase ZECs in the following period will be reduced.

REHEARING AND RECONSIDERATION ARE REQUIRED

I. Adoption of the ZEC Program Is Outside The Commission's Delegated Scope of Authority.

In creating the ZEC Program, the Commission exceeded the scope of its delegated authority and transgressed the "difficult-to-define line between administrative rulemaking and legislative policy-making" *Boreali v Axelrod* (71 NY2d 1, 11-14 [1987]). In New York, the Legislature cannot delegate its lawmaking power to an administrative agency (NY Const, art III, § 1; *see*, *Matter of Nicholas v Kahn*, 47 NY2d 24, 30-31 [1979]). Nor may another branch of

government "arrogate unto itself the powers residing wholly" in the Legislature (*id.,* 47 NY2d at 31). Although the Commission may act in a manner "combining legislative, executive and judicial functions, [it is] but a creature of the Legislature and possessed only of those powers expressly or impliedly delegated by that body" (*id.* [citations omitted]). Commission action is limited to the task of "fill[ing] in the interstices in the legislative product by prescribing rules and regulations consistent with the enabling legislation" (*id.*; *Boreali v. Axelrod*, 130 AD2d 107).

The Commission's enabling legislation is found in the Public Service Law and its animus is the goal of providing the public with adequate utility services at just and reasonable rates (*see*, PSL §§5 and 66). When, as here, the Commission "attempts to resolve difficult social problems by making choices among competing ends" without legislative guidance, it oversteps its bounds (*Matter of New York Statewide Coalition of Hispanic Chambers of Commerce v New York City Dept. of Pub. Health & Mental Hygiene*, 23 NY3d 681, 697 [2014]). "That task, policymaking, is reserved to the legislative branch" (*id.*). Because the ZEC Program represents a choice by the Commission among competing ends – maintaining lower utility rates versus lowering carbon emissions – only one of which, the level of utility rates, lies within the scope of its legislative delegation, it is beyond the purview of the Commission's delegated authority. That the policy choice the Commission made requires the dramatic departure from existing market structures and regulatory policies that the ZEC Program represents demonstrates just how far afield the Commission has strayed from its delegated scope of authority. Just as eliminating smoking in public indoor areas was a dramatic departure from previous practices that would "affect how millions of New Yorkers live their lives" (*Boreali v Axelrod*, 130 AD2d 107, 114 [3d Dept 1987], *affd* 71 NY2d 1 [1987]), the Commission's decision to interfere with market forces (discussed *infra*, Part II) will affect how millions of New Yorkers pay for electricity. "Such

dramatic changes in public policy, however meritorious in terms of the public health, are, the function of the Legislature, not an administrative agency" (*id.)*.

Here the Commission has advanced a specific energy source – nuclear power generated by four upstate plants – while closing-off to public debate myriad and complex questions relating to community concerns and alternative energy choices. And it has arrogated to itself the task of assigning a monetary value to the social cost of carbon emissions. The Commission has taken this extreme step, under the auspices of its authority to "encourage... the preservation of environmental values and the conservation of natural resources" (*See* PSL §5[2]). But, settling by rule having the force of law such a complex social policy question with far reaching effects upon individual communities, the State's energy markets and the State's business environment, requires far more explicit guidance than the exhortation provided in PSL § 5(2). Because these policy decisions have been made without legislative guidance they must be reconsidered.

In *Boreali*, the Court of Appeals identified four "coalescing circumstances" to identify whether an agency has gone too far into the policy-making realm (71 NY2d at 11-14). These categories continue to be the "touchstone for determining whether agency rulemaking has exceeded the legislative fiat" (*Matter of NYC C.L.A.S.H., Inc. v New York State Off. of Parks, Recreation & Historic Preserv.*, 27 NY3d 174, 178 [2016]). Accordingly, we ask: (1) did the agency make "value judgments entail[ing] difficult and complex choices between broad policy goals to resolve social problems"; (2) did it write on "a clean slate, creating its own comprehensive set of rules without benefit of legislative guidance"; (3) has the legislature "unsuccessfully tried to reach agreement on the issue"; and (4) did the agency use "special expertise or competence in the field to develop the challenged regulation?" (*id.*, *citing Greater N.Y. Taxi Assn. v New York City Taxi & Limousine Commn.*, 25 NY3d 600, 610 [2015]; *Matter*

of New York Statewide Coalition of Hispanic Chambers of Commerce v New York City Dept. of Health & Mental Hygiene, 23 NY3d 681, 698 [2014]). While no single factor is dispositive or required, the simple question raised by all four is whether, when viewed collectively, the agency has acted outside its statutory mandate (*see Ellicott Group, LLC v. State of N.Y. Exec. Dept Off. of Gen. Servs.*, 85 AD3d 48, 54 [4th Dept 2011]). Here the answer is "yes."

The record shows that all four *Boreali* factors are present and that the Commission overstepped its broad powers to regulate electric utilities by exercising "'open-ended discretion to choose ends', which characterizes the elected Legislature's role" (*Boreali*, 71 NY2d at 11 [citation omitted]). This "open-ended discretion" manifests itself in two specific ways: (1) by deciding to preserve only the "at risk nuclear zero emissions attributes" without consideration of other low and zero-emission resources (*August 1 Order* at 2) so that those sources do not succumb to competitive market pressures; and (2) by adopting the Social Cost of Carbon as the metric to establish the value of the benefit of electricity generation from un-economic nuclear generating facilities. Because the ZEC Program, in its current form, exhibits all of the same problems as the rules struck down in *Boreali* and *Coalition of Hispanic Chambers*, it must be deemed as equally unacceptable.

A. The Commission's ZEC Program Is Simultaneously An Exercise of Broad Policy-Making and Policy Implementation Without Legislative Guidance; It Is Not An Act of Regulation Within The Commission's Circumscribed Sphere.

In adopting the ZEC Program the Commission has strayed too far afield. The admitted impetus of the ZEC Program is the Commission's desire to counter the natural effects of competition in the wholesale power markets, "particularly low natural gas prices [that] have benefitted consumers but have impaired the financial viability of upstate nuclear plants, to the point where plant owners have announced the intention to close plants that are otherwise fully

licensed and operational" (*August 1 Order* at 45). The ZEC Program's stated ends are not lower rates or improved services, but environmental and social – "to avoid backsliding in the State's efforts to reduce carbon emissions" (*id.* at 45). In fact, because ZEC payments are above market, they will result in increased rates (*id.* at 127-128). In narrowly focusing on the four upstate nuclear generating facilities, rather than all zero emission sources, the Commission carved out an exception to existing market-based rules. Further, the Commission rejected the original staff proposal to use "anticipated operating costs of the plants and anticipated wholesale energy prices of energy" to set the price of ZECs and, instead incorporated an un-vetted metric – "a formula that begins with published estimates of the social cost of carbon" (*August 1 Order* at 49). Accordingly, the ZEC Program is an explicit attempt by the Commission to weigh the competing social concerns of combating global warming against controlling the cost of electricity, but without any legislative guidance on how to balance those competing concerns.

The ZEC Program and adoption of the Social Cost of Carbon is invalid because it is fundamentally focused on environmental concerns, which the Legislature has not delegated to the Commission. The Legislature has placed this function squarely and explicitly within the Environmental Conservation Law (ECL) and in the purview of the New York State Department of Environmental Conservation. Accordingly, the Commission's efforts to broaden its powers in the environmental sphere are inappropriate (*see* ECL §§ 1-0101 and § 3-0301). In *Ellicott Group, LLC v State of N.Y. Exec. Dept. Off. of Gen. Servs.,* 85 AD3d 48 (4th Dept 2011), the court explained that the Office of General Services (OGS) violated the separation of power doctrine by attempting to "broaden" its authority to areas beyond that prescribed by the Legislature. In rejecting attempts to increase the circumstances where prevailing wage would be required, OGS had exceeded its authority because it had gone beyond the "parameters" set by the

Legislature (85 AD3d at 353). As the court explained, this attempt to expand the agency's power was invalid because this was an "area of the law that continue[d] to evolve, and it [was] the role of the Legislature to make any such changes, not the role of an administrative agency (*id.* at 54).

This type of agency value-choosing was deemed inappropriate in both *Boreali* and *Coalition of Hispanic Chambers,* 23 NY3d at 698 (*citing Boreali*, 71 NY2d at 12). In *Boreali*, as here, the Public Health Council (PHC) sought to regulate an environmental condition to advance the "laudable goal of protecting non-smokers from the harmful effects of 'passive smoking'" (71 NY2d at 11). But, in doing so, the PHC improperly weighed "the goal of promoting health against the social cost" by relying on "administratively created exemptions rather than on rules that promote the legislatively expressed goals" (*Boreali,* 71 NY2d at 12*).* As noted by the Court, when the created exemption runs counter to a legislative goal, it "cannot be justified as simple implementation of legislative values" (*Id.*, *citing Khan*, 47 NY2d 24). Similarly, in *Coalition of Hispanic Chambers*, the Board of Health (BOH) attempted to reduce the consumption of sugary drinks by crafting a program that narrowly targeted one particular type of service provider (23 NY3d at 698). This narrow focus required a series of choices between different ends and "more than simple balancing of costs and benefits according to pre-existing guidelines" (*id.*). Here, the Commission has chosen to target only upstate nuclear power generation and has dismissed or rejected the numerous commenters who objected vigorously to the maintenance of these facilities (*see e.g.,* Comments of Assemblywoman Ellen C. Jaffee and Assemblywoman Barbara Lifton [*August 1 Order*, Appendix B at 16 and 17]). In turn, the Commission has both excluded other zero-emissions generation from the ZEC Program and exempted the nuclear generation facilities from the economic effects of competition in the wholesale market. Nor has the Commission evaluated the full range of impacts resulting from subsidizing these units. Therefore, by using a

metric beyond its own expertise to subsidize a narrow group of generators, the Commission has necessarily engaged in the process of choosing between competing public-policy ends and broad policy goals – a task reserved to the Legislature.

B. The Commission has Created the ZEC Program on a "Clean Slate"

The ZEC Program is unique because it represents a virtual first-in-the nation attempt by a public utility commission to subsidize a particular electric generation source based upon the social cost of (avoided) carbon emissions. But this very characteristic compels scrutiny of the Commission's effort. As in *Boreali*, this application for rehearing does not challenge the wisdom of such a program or the authority of government in general to propose such a measure (72 NY2d at 8). Nor is the veracity of climate change science pertinent beyond providing the relevant context (*see id.*). Instead, we ask only whether the general grants of authority found in PSL §§5 and 66 are sufficient to support the extreme and disruptive measures adopted here.

In *Boreali*, the Court found that the PHC wrote its antismoking regulation on a "clean slate, creating its own comprehensive set of rules without benefit of legislative guidance" because it "did not merely fill in the details of broad legislation describing the over-all policies to be implemented" (*see* 71 NY2d at 13). The Commission does not even claim that the ZEC Program is the type of "'interstitial' rulemaking that typifies administrative regulatory activity" (*Boreali*, 71 NY2d at 13). Instead, the Commission has created a new program to raise additional revenue for a specific class of generators that would otherwise have succumbed to competitive market forces. This very characterization reveals the Commission's lack of legislative direction.

The Commission's price-setting mechanism also departs fundamentally from the Commission's traditional cost-of-service models, which rely on objective standards uniquely

capable of verification. This creates even more need for additional scrutiny because the Commission does not attempt to explain the exclusion of other zero emission resources from the ZEC Program, such as small-scale hydro-power or wind or solar resources. As a result, the ZEC Program has a narrow focus that cannot be reconciled with the stated goal of preserving zero emissions electricity. When evaluated by the Social Cost of Carbon, electricity from solar, wind, and hydro-electric resources have the same value as the carbon emissions offset by continued use of nuclear power. New York's courts have rejected such arbitrary distinctions in the past. *E.g., Matter of Law Enforcement Officers Union Dist. Council 82, AFSCME, AFL-CIO v. State of New York*, 229 AD2d 286, 289-90 (3d Dept 1997) (improperly distinguished between types of inmate housing units); *Matter of Kelly v. Kaladjihan*, 155 Misc 2d 652, 657-58 (Sup Ct, NY County, 1992) (improperly drew distinctions that were unrelated to agency's goal).

In the *August 1 Order*, the Commission also points to the Energy Law and the State Energy Plan, as support for its claimed authority. But these provisions must be examined in light of the goals of the Public Service Law. As the Court cautioned in *Boreali*, "a legislative grant of authority must be construed, whenever possible, so that it is no broader than that which the separation of powers doctrine permits" (71 NY2d at 9). Accordingly, these powers cannot be interpreted as license to adopt the Social Cost of Carbon as the correct metric for making value judgments about the continued use of nuclear energy, or the value of emissions from any particular source of energy. To do so would improperly expand the Commission's authority to regulate economic activity and would lead to more value-laden decisions. This is a power that goes beyond "encouraging" environmental stewardship or establishing "just and reasonable" rates.

C. The ZEC Program Intrudes Upon An Area Of Legislative Debate.

The fate of New York's upstate nuclear generation fleet has been a recurring topic of public discourse. It has been widely reported that the Governor's office brokered efforts to prevent the closure of several upstate facilities and the Commission readily admits that it has been encouraged, or even directed, by the Executive Chamber to preserve the upstate nuclear facilities (*see August 1 Order* at 6). This too is more cause for scrutiny because it betrays a failure to achieve a legislative solution to a recognized social issue: the failing economics of upstate nuclear power generation. As *Boreali* made clear,

> failures by the Legislature to arrive at such an agreement do not automatically entitle an administrative agency to take it upon itself to fill the vacuum and impose a solution of its own. Manifestly, it is the province of the people's elected representatives, rather than appointed administrators, to resolve difficult social problems by making choices among competing ends

(*id.*, 71 NY2d at 13). Nor does support of the executive provide the necessary authority (*see Under 21, Catholic Home Bur. for Dependent Children v City of New York,* 65 NY2d 344, 353 [1985] [finding Mayor lacked authority to issue executive order that broadened the class of persons protected by the enabling statute]).

D. The ZEC Price Formula is Not the Product Of The Commission's Special Technical Expertise.

The Commission lacks the technical expertise to determine whether the Social Cost of Carbon is an appropriate counterbalance to the social cost of nuclear power generation. In *Boreali*, the Court acknowledged that the PHC unquestionably possessed the authority to deal with matters affecting public health, and that it had thoroughly addressed the available scientific evidence pertaining to the dangers of environmental tobacco smoke (71 NY2d at 6). The Court nonetheless determined that the agency exceeded its authority because no special expertise was

involved in the "development of the... regulations challenged" (*id.* at 14 [emphases added]). The same is true here. The Commission simply seized on the estimate made by a federal interagency working group of the Social Cost of Carbon in order to arrive at a formula for calculating the amount of subsidy it desired. It did so with little apparent analysis or deliberation and without resort to its expertise in utility costs. Whether the Commission made its choice as a convenience or for some other reason, it is undeniable that the metric is not the product of its expertise in the regulation of public utilities.

II. By Adopting The ZEC Program The Commission Would Regulate The Wholesale Market Which Is Exclusively Within The Jurisdiction Of The Federal Government.

A. FERC Has The Exclusive Authority To Set Wholesale Rates.

The "pre-emptive impact of federal jurisdiction over wholesale rates on state regulation" is beyond debate (*Miss. Power & Light Co. v. Miss.*, 487 US 354, 371 [1983] *citing Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 [1986]). Although both *Miss. Power & Light* and *Nantahala Power & Light* concerned attempts by state utility commissions to exclude from retail rates the full recovery of wholesale rates set by FERC, there is nothing in the well-established law that would authorize states to *increase* wholesale rates by adding a premium to FERC-approved wholesale rates and requiring that wholesale purchasers pay the premium. Wholesale rates in New York's "fully restructured" (*August 1 Order* at 10) electric industry are set in competitive markets administered by NYISO pursuant to FERC-approved tariffs (*see Hughes v. Talen Energy Mktg., LLC,* 578 US __ [2016] Slip Op at 3-4). "FERC has the exclusive authority to determine the reasonableness of wholesale rates" (*Miss. Power & Light*, 487 US at 371), and exercises its exclusive authority by prescribing, approving and enforcing the NYISO tariffs. A state program that "functionally sets the rate that [a wholesale generator] receives for its sales [in a] "FERC-approved market mechanism... strikes at the heart of

[FERC's] statutory power" (*Hughes v. Talen,* 578 US ___, Slip Op at 10, *citing PPL Energy Plus, LLC v. Nazarian,* 753 US Fed 467, 476 (2014). By directing the New York LSE's to effectively purchase the amount of power generated by the upstate nuclear facilities needed to support the ZEC's each must purchase, the ZEC Program intrudes into pre-empted terrain for an independent reason, because "FERC's exclusive jurisdiction applies not only to rates but also to power allocations that affect wholesale rates" (*Miss.* 487 US at 371).

In the *August 1 Order,* the Commission suggests that the ZEC Program passes through the door left open in *Hughes v. Talen* for state initiatives that "encourage development of new or clean generation" by measures "untethered to a generator's wholesale market participation" (*Hughes v. Talen,* 578 US __ Slip Op at 15). Contrary to the assertion in the *August 1 Order* that the ZEC "model more closely ties the pricing mechanism for ZECs to the environmental attributes, leaving no doubt that it falls squarely within the State's exclusive jurisdiction" (*August 1 Order* at 151), as described below, the ZEC model adopted by the Commission directly intrudes on FERC's exclusive jurisdiction.

B. The ZEC Program Interferes with the Operation of a Market Within FERC's Pre-emptive Jurisdiction.

Under the ZEC Program, LSEs, who must of necessity purchase power in the wholesale market to meet their customers' collective needs, will be compelled to pay out-of-market payments for power supplied in the wholesale market by the owners of four upstate nuclear power plants.[1] The ZEC Program is aimed at maintaining historic levels of power production from these specific plants, which if left to the competitive wholesale market would not survive and would be shut down and retired. Clearly the Commission is not satisfied with the operation

[1] The upstate nuclear plants are treated, for regulatory purposes, as Exempt Wholesale Generators, which frees them from cost-of-service rate regulation. As discussed in Part IV *infra*, that status is called into question by their participation in the ZEC Program.

of the competitive wholesale market and has resorted to direct interference in that market to correct what dissatisfies it.

In a fully integrated utility model subject to traditional cost-of-service regulation, the market forces giving rise to the Commission's adoption of the ZEC Program would not have been brought to bear and the vertically integrated utility-owners of the upstate nuclear facilities would have received cost-of-service-based rate increases that would keep the nuclear plants operating, immune from the effects of competition, including lower natural gas prices and new, more efficient power generation. As acknowledged by the Commission (*August 1 Order* at 9-10), New York chose to restructure the electricity market and to rely on the wholesale market regulated by FERC for purchase and sale transactions at the wholesale level. The *August 1 Order* acknowledges that it is the outcome of the operation of that market that prompted the Department of Public Service (DPS) to offer the initial ZEC proposal, which was described as necessary to assist in the transition "from nuclear to non-nuclear resources if wholesale prices remain too low to support the existing nuclear plants" (*August 1 Order* at 45-46).

Although the Commission implies that the ZEC Program is "untethered" to the participation of the upstate nuclear plants in the wholesale market (*id.* at 69 *citing Talen*), that is simply not the case. The shift from the initial DPS ZEC proposal, in which ZECs would be based on the nuclear plants' operating costs, to the program adopted in which ZECs are based on the Social Cost of Carbon does not free the program from its fundamental flaw: entangling the State in an area federally pre-empted. This is not a case in which New York State is providing a direct subsidy paid from New York's general fund to the plant owners, whether based on a desire to support their environmental attributes or their local employment benefits. The ZEC Program directly inserts the Commission into the administration of the wholesale markets by: (i)

modifying the prices received by the nuclear plants for wholesale sales; (ii) directing LSE's as to what power resources to purchase from, in what quantities, and how much to pay for such power in the wholesale market; and (iii) consequently interfering with the normal functioning of the wholesale markets for both capacity and energy.

1. ZEC Revenues To Be Received By The Nuclear Plant Owners Would Be The Result Of Wholesale Prices Set By The Commission.

The *August 1 Order* characterizes the ZEC payments and receipts as disbursements paid, and revenues earned, from the sale of a distinct product – zero-emissions attributes – created by the Commission purportedly acting pursuant to state authority. That characterization cannot disguise that the ZEC Program adds an administratively determined premium to the competitively set price to overcome the Commission's dissatisfaction with the natural operation of the wholesale marketplace. The *August 1 Order* discloses that by identifying ZECs as a product supposedly distinct from the electricity produced by the nuclear plants the Commission believed it would fend off a pre-emption challenge (*id.* at 119, 151). But, the price premium is imposed as a part of a directive telling the plant owners how much electricity to produce for wholesale and telling the wholesale purchasers how much to buy from, and what to pay, the plant owners. The nuclear plant owners only receive the premium if they produce electricity and their continued eligibility depends on their producing electricity in prescribed quantities. Finally, the calculation of the ZEC is itself directly pegged to forecasts of what prices will result in the competitive wholesale market. Thus, for the second through sixth contract periods (years 3-12) the ZEC will be set at the forecast Social Cost of Carbon less the amount already embedded in the expected market revenues of $39.00. Thus the Commission has made estimates of what revenues the upstate nuclear plants will recover in the competitive market and has administratively established an above-market premium to be received by the owners in wholesale

rates. It is beyond reasonable debate that the ZEC "program sets an interstate wholesale rate, contravening the [Federal Power Act's] division of authority between state and federal regulators" (*Hughes v Talen,* Slip Op at 12).

2. The Prices Paid By LSE's To Purchase ZECs And The Quantity Of Upstate Nuclear Power To Be Purchased By LSEs Would Be The Result Of Wholesale Rate Setting And Power Allocations Mandated By The Commission.

LSE's today buy power in the competitive wholesale market, in which they are free to buy in the NYISO-administered markets or in bi-lateral contracts, including bilateral contracts designed to meet their special needs, such as purchasing only from certain technologies or meeting long-term price stability needs of their customers. Under the ZEC Program LSE's are mandated by the Commission to purchase, regardless of whatever else they purchase, power produced by four upstate nuclear facilities, in mandatory quantities, at an administratively-determined prices. In the ZEC Program the Commission will set the wholesale rate to be paid by the LSEs and will mandate the allocation of power to be purchased in a manner that affects the wholesale rates they pay, both in clear violation of *Mississippi Power & Light*, 487 US 354, 371 (1983).

3. The ZEC Program Will Interfere With The Creation Of Accurate Price Signals That Are Critical To A Properly Functioning Capacity Market.

In a competitive market, the conditions facing the upstate nuclear plants would cause their owners to retire them from service. The market's loss of their capacity would put upward pressure on the cost of capacity offered in the NYISO-administered capacity markets. This, in time, would lead to new capacity coming into the New York capacity markets. The ZEC Program will suppress this market signal, interfering with the normal functioning of the federally-regulated wholesale power market.

State-supported subsidies paid to keep uneconomic generators running have been identified by FERC as impediments to the working of competitive wholesale markets (*Hughes v Talen*). A core element of the ZEC Program is a presumption that the nuclear facilities will earn energy and capacity revenues from the NYISO markets, because the proposed pricing formula decreases the ZEC price to the extent projected average energy and capacity revenues in subsequent years exceed the average energy and capacity prices of $39/MWh. The implicit presumption is that the subsidized nuclear facilities will offer their capacity in the NYISO's ICAP auction as price takers at below-cost, to ensure their offers clear because they must rely on the sum of energy market revenues, capacity revenues and the ZEC subsidies to cover their costs to continue operating.

Such below-cost offers will severely depress capacity prices, a textbook example of how the exercise of buyer-side market power works. The ZEC Program would retain uneconomic nuclear facilities in the competitive market with out-of-market ZEC payments with the unavoidable result of artificially suppressing energy and capacity prices. Indeed, a report by The Brattle Group, issued in 2015, stated that, absent the upstate nuclear facilities, "average electricity prices in New York would increase by about $10/MWh on a wholesale basis" (*New York's Upstate Nuclear Power Plants' Contribution to the State Economy,* The Brattle Group [December 2015] at 8). Interference with the function of the wholesale market cannot be excused because the particular type of interference at issue produces (in the short term) desirable results.

C. The State's Authority Regarding Electricity Generation May Not Be Exercised In Ways That Interfere With The Operation of Wholesale Markets.

New York State has the authority, free of challenge based on federal pre-emption, to decide whether to license power plant construction and, in doing so, which technologies, fuel sources and environmental attributes to favor. Where, however, a state acts in ways that affect the operation of, or the activities within, the wholesale market, its authority has severe limits. For example, buyer-side mitigation rules imposed by NYISO and upheld by FERC demonstrate that the economic and financial operation in the wholesale market of electric infrastructure projects, although licensed by the state, nevertheless can be effectively regulated by the federal scheme in ways not necessarily anticipated by the State when it licensed them. *See, e.g., Hudson Transmission Partners, LLC v New York Independent System Operator*, 145 FERC ¶ 61,156 (2013), *Order Denying Complaint* and 153 FERC ¶ 61,191 (2015) *Order on Rehearing Clarification and Compliance Filing.*

The Commission has implicitly acknowledged the overarching authority of the federal scheme that relies on competitive forces when it has exercised its undeniable authority to grant licenses for new transmission lines and natural gas-fired power plants. *See, e.g.,* Case 10-T-0139, Champlain Hudson Power Express, *Order Granting Certificate of Environmental Compatibility and Public Need* (April 18, 2013) at 41:

> by granting the Facility a certificate, we are providing its investors with the option to move forward with construction of the Facility if circumstances such as a revised gas price forecast lead its investors to believe that it will be an economic project... If the economics are positive and the Project is built, then society will be better off for it, because of the important non-monetary benefits. If the economics become worse and the Project never gets underway, then no harm will come of our decision to grant the Facility a certificate.

Thus, even in the course of exercising its exclusive authority to license new wholesale infrastructure, the Commission has accepted that the licensed infrastructure will operate (or not) in a wholesale market that is exclusively governed by competitive economics. But, in adopting the ZEC Program, the Commission has embarked on an untenable course in which the wholesale electricity market will be a shared responsibility of FERC and the Commission.

III. The ZEC Program Burdens Interstate Commerce.

By compelling LSE's operating in an otherwise competitive wholesale interstate market to purchase ZECs that are produced exclusively by four upstate nuclear plants in compelled quantities, the Commission is favoring New York State-produced electricity at the expense of electricity produced and transmitted in interstate commerce. Prior to the *August 1 Order*, LSE's operating in New York State could meet their customers' needs by freely purchasing from both in-state and out-of-state sources, the latter being constrained only by the physical limits of the interstate transmission paths and the associated scheduling requirements.

The *August 1 Order* puts the thumb of New York State on the scales of interstate commerce in wholesale power by compelling wholesale purchasers to buy a fixed amount of their needs only from four upstate nuclear plants. At its core, the ZEC Program is a financial subsidy intended to preserve an existing market for electric energy produced by four specific upstate nuclear power generating units. By design, it is simple economic protectionism. It does not regulate evenhandedly, but targets a narrow commodity and excludes from participation all out-of-state electric generating resources, including similarly situated out-of-state "zero-emissions" nuclear generating resources, simply because of their location (*see*, *Loretto Winery, Ltd. v Gazzara*, 601 F Supp 850, 856 [SDNY 1985], *citing Philadelphia v New Jersey*, 437 US 617, 622 [1978]). As a result, the ZEC program unlawfully discriminates against, and unduly

burdens, interstate commerce in electricity generally, and in zero emission electricity specifically.

Economic protectionism effectuated by state legislation or administrative action is subject to a "virtual *per se* rule of invalidity" (*id.*). That the ZEC Program is economic protectionism is without question. As the Commission declared, "ZECs provide a vehicle for monetizing the State's environmental preferences... " (*August 1 Order* at 20), and the adoption of the ZEC Program was urged by the governor for the express purpose of saving in-state economic resources from the vagaries of competitive wholesale interstate markets. In *Loretto Winery*, the State legislature amended portions of the Alcohol Beverage Control (ABC) Law to allow certain wine drinks – made only from in-state grapes – to be sold in grocery stores. Like the ZEC Program here, the ABC regulation did not prevent identical out-of-state wine products from being sold in New York, but excluded them from the significant advantage pertaining to grocery-chain distribution. The stated purpose of the law was to "provide significant assistance to the [New York wine and grape] industry which is extremely important to New York State" (*id.* at 857). Accordingly, even in light of the broad authority granted the State under the 21st Amendment to regulate the import of alcoholic beverages, the statute was invalid because it did not regulate the product of local and out-of-state industries evenhandedly (*id.* at 858). The ZEC Program is equally invalid because it results in a similar prohibited circumstance, where purchasers of electricity are forced to purchase an "equivalent product" from in-state resources (*Id.*).

Administrative action that protects local industry is equally infirm. In *Farmland Dairies v Commissioner of New York State Dep't of Agriculture & Markets*, 650 F Supp 939 (EDNY 1987), the court struck down a regulation which had the intended purpose of protecting local

milk producers. The regulation at issue allowed the Commissioner to deny a license to milk dealers if "the issuance of the license will tend to a destructive competition in a market already served; or... that the issuance of the license is not in the public interest" (*id.* at 941). Noting that the underlying purpose of the regulation was based on economic protectionism, the court found the regulation invalid regardless of whether it was to prevent loss of revenue or "rooted in concern that an adequate supply of milk be available for New York consumers" (*Id.* at 943). The ZEC Program is likewise a violation of the Commerce Clause because it is, at its core, economic protection, regardless whether its goal is characterized as preventing a loss of revenue for upstate nuclear power plants or as ensuring an adequate supply of zero-emission megawatts to New York ratepayers.

IV. The Commission Has Failed to Provide Reasoned Explanations for Several Key Aspects of Its Order.

In 1996, the Commission concluded that competitive markets provide rates for electric services that are just and reasonable. Case 94-E-0952, Opinion No. 96-12, *Opinion and Order Regarding Competitive Opportunities for Electric Service* (May 20, 1996):

> Competition in the generation and energy services sectors of the electric industry will be pursued for its potential to reduce rates over the long term, to increase customer choices, and for other economic development advantages.

(Opinion No. 96-12 at 96). In supporting competition as the guiding force motivating electricity markets, the Commission has accepted that the wholesale markets for energy and capacity in New York State are regulated exclusively by FERC and administered by the NYISO through its Open Access Transmission Tariff and Market Services Tariff, tariffs that are reviewed and approved and made effective by the FERC.

The Commission's dedication to competitive markets has been evident in numerous policy statements, orders and licensing decisions. The Commission has observed that its dedication to competition at the wholesale level has produced savings for consumers as those markets have directly brought to consumers the benefits of the downward pressure on prices due to the abundant supplies of natural gas, the efforts of power generators supplying the New York market to keep operating costs down and the efforts of power plant designers to bring ever more efficient power plants online. *See, e.g.,* Case 14-M-0101, *Order Adopting Regulatory Policy Framework and Implementation Plan*, February 26, 2015 at 19.

By the *August 1 Order*, the Commission has decided that when it is not satisfied with a particular consequence of the normal operations of the competitive wholesale market – in this case the fact that wholesale prices and, therefore revenues, have been driven so low as to threaten the economic usefulness of four upstate nuclear plants – it may step in to provide a "correction." The correction in this case will require New York's consumers to transfer billions of dollars to the owners of those plants, who in turn, it is hoped, will maintain their labor forces and continue infusing funds into their local economies.

The *August 1 Order* represents a dramatic and abrupt departure from well-established regulatory structures and policy choices. Nevertheless, the *August 1 Order* includes no reasoned explanation for: (i) its divergence from existing policies and regulatory structures; (ii) what the follow-on implications of that divergence will be; (iii) how the Commission will reconcile the new paradigm facing wholesale market participants in New York with existing and, presumably, to-be-continued rules governing that market, and (iv) the reasonableness or accuracy of the federal agencies' Social Cost of Carbon metric.

For two decades the Commission has put its faith in, and has shaped the electric utility industry around, reliance on competitive forces and consumer choice. In one act, the adoption of the ZEC Program, the Commission has pulled the rug out from under its long-standing commitment to both with no reasoned explanation other than the expression of a desire to continue the operation of the four nuclear plants for environmental purposes. Missing, for example, are explanations of how the pros and cons of making such a dramatic change were weighed and of whether and by what rationale the Commission might use a similar approach for some other policy goal. The change from the Commission's prior endorsement of free markets and maximizing consumer choices and the resulting damage to the competitive markets which depend on stability and uniformly applied rules are too great to be supported with such little explanation. The Commission has engineered this "correction" without giving any explanation reconciling it to its policies committing the State to the forces of competition in the wholesale electric markets.

The Commission has not even acknowledged how its own practices in infrastructure licensing have helped to create the competitive market forces that have resulted in the upstate nuclear plants facing closure. In a full embrace of competition, the Commission's practice has been to license new projects by finding that they serve the public need by providing benefits in the form of reduced costs for ratepayers achieved by increasing the supply of electricity and competition, notwithstanding the likely negative, consequent impact on the ability of nuclear plants to operate in the market. For example, in granting a certificate for the Champlain Power Hudson Express project, the Commission observed,

> As for any impact of the Facility on incumbent generators, be they New York City generators or upstate generators, we acknowledge that the Facility will result in lower wholesale market prices, albeit for only a temporary period. Therefore, as in any well functioning

> market, the entry of a new supplier will likely impact incumbent suppliers. *This is an effect that is more than tolerable as a consequence of the proper workings of a competitive market.*

(Case 10-T-0139, *Order Granting Certificate of Environmental Compatibility and Public Need* (April 18, 2013) at 51-52 [emphasis added]). Similarly, in licensing a new gas-fired generator the Commission concluded:

> The Project would incorporate high-efficiency combined-cycle technology, and is expected to enhance electric system reliability by adding a new generation resource and increasing fuel diversity in the region and providing congestion relief. Given these anticipated benefits, we reject the suggestions raised by certain commenters that surplus generation exists in the upstate region and that the Project is not needed.

(Case 10-E-0501, CPV Valley, LLC, *Order Granting Certificate of Public Convenience and Necessity, Authorizing Lightened Ratemaking Regulation, and Approving Financing* [May 9, 2014] at 15-16). The Commission has frequently cited "enhancing competition" as a basis for finding that a proposed new power plant is "necessary and convenient for the public service." *See, e.g.,* Case 05-E-0098, Caithness Long Island, LLC, *Order Granting a Certificate of Public Convenience and Necessity, Providing for Lightened Regulation and Approving of Financing* (November 15, 2006).

The *August 1 Order* even fails to discuss the impact of the ZEC Program on the market status of the upstate nuclear plants. When the Commission authorized the transfer of the upstate nuclear facilities from their original, fully-regulated, utility owners, the Commission explicitly and purposefully facilitated the new owners' ability to be treated by FERC as Exempt Wholesale Generators, and granted them lightened regulatory status for New York State purposes. *See, e.g.,* Case 01-E-0011, Joint Petition of Niagara Mohawk Power Corporation, New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, Central Hudson Gas & Electric

Corporation, Constellation Nuclear, LLC and Nine Mile Point Nuclear Station, LLC for Authority Under Public Service Law Section 70 to Transfer Certain Generating and Related Assets and for Related Approvals, *Order Authorizing Asset Transfers* (October 26, 2001) at 23-24 [footnotes omitted]):

> In conformance with PUHCA and FERC's regulations, the Commission finds that allowing the Nine Mile facilities to become eligible facilities, with Constellation owning the plants (either directly or indirectly through one or more affiliates as defined under federal law) will benefit New York consumers, is in the public interest, and does not violate New York law.
>
> These findings are made on the same basis that we have found that the transaction is in the public interest pursuant to PSL §70. The Commission determined in Case 94-E-0952 (Opinion No. 96-12) that a competitive marketplace for the provision of electricity supply would benefit New York customers and this transaction furthers that goal.

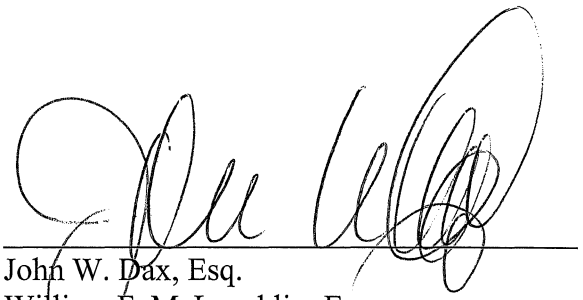
There the Commission acknowledged that, once divested from their utility owners, the nuclear plants were to be full participants in the wholesale power markets, subject to the competitive market forces over which the Commission has no jurisdiction. Again, the *August 1 Order* includes no reasoned explanation for the change in policy, of what it may portend for the future of the electric industry in New York or what it means for the owners of the affected nuclear facilities.

We do not contend that the Commission is locked into policies and regulatory structures previously adopted. However, when it departs in as dramatic a manner as evident in the ZEC Program, the Commission owes the public, and those who have made significant investments based on prior policies, a thorough and well-reasoned discussion.

CONCLUSION

For the reasons expressed, the Commission should grant rehearing and upon rehearing reconsider its adoption of the ZEC Program.

Dated: August 31, 2016

By: 

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