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November 19, 2015

VIA EMAIL ONLY: secretary@dps.ny.gov

Hon. Kathleen H. Burgess
Secretary to the Commission
New York State Department
of Public Service
Three Empire State Plaza
Albany, New York 12223-1350

Re: Case 14-E-0270 - Petition Requesting Initiation of a
Proceeding to Examine a Proposal for Continued
Operation of the R.E. Ginna Nuclear Power Plant, LLC.

Dear Secretary Burgess,

Attached please find the Department of Public Service
Staff's Statement in Support of the Joint Proposal filed in the
case captioned above. Should you have any questions, please do
not hesitate to contact me.

Very truly yours,

s/ *Alan T. Michaels*

Alan T. Michaels
Assistant Counsel

Attachment

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 14-E-0270 - Petition Requesting Initiation of a Proceeding
to Examine a Proposal for Continued Operation
of the R.E. Ginna Nuclear Power Plant, LLC.

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE STAFF
STATEMENT IN SUPPORT OF JOINT PROPOSAL

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Dated: November 19, 2015
Albany, New York

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE COMMISSION

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NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE STAFF
STATEMENT IN SUPPORT OF JOINT PROPOSAL

INTRODUCTION

R.E. Ginna Nuclear Plant, LLC (Ginna) initiated this proceeding when it filed a Petition containing a proposal for the continued operation of the R.E. Ginna Nuclear Power Plant (the Facility). The Petition stated that Ginna's owner, Constellation Energy Nuclear Group, LLC, had determined that the expected forward-looking revenues from the Facility's sale of capacity and energy would not be sufficient to cover its costs of continued operation, including required new capital investment.

The Facility is a 581 MW single-unit pressurized water reactor located along the south shores of Lake Ontario, in Ontario, New York, approximately 20 miles northeast of Rochester, New York. In 2004, the federal Nuclear Regulatory

Commission extended the Facility's license to operate until September 2029.¹

Following the petition, the parties conducted extensive discovery and negotiations resulting in a Joint Proposal containing terms for the continued operation of the Facility. The terms of the Joint Proposal support Commission policies and strike a balance between the interests of customers and investors. Additionally, the terms of the Joint Proposal compare favorably with the likely outcome of litigation. Accordingly, the Joint Proposal meets the Commission's criteria for settlements; it is therefore just, reasonable, and in the public interest.² As a result, it should be recommended that the Commission adopt the Joint Proposal.

BACKGROUND

On July 11, 2014, Ginna filed a Petition requesting initiation of a proceeding to examine a proposal for continued operation of the Facility. Specifically, Ginna sought: (1) a finding that continued operation of the Ginna Facility is necessary for electric service reliability; (2) a determination that its Petition satisfies the requirements for giving notice

¹ Issuance of Renewed Facility Operating License No. DPR-18 for R.E. Ginna Nuclear Power Plant, Operating License, Nuclear Regulatory Commission, (issued May 19, 2004).

² Cases 90-M-0225 and 92-M-0138, Opinion, Order and Resolution Adopting Settlement Procedures and Guidelines, Opinion No. 92-2 (issued March 24, 1992), p.30.

of a proposed retirement; and, (3) an Order directing Rochester Gas and Electric Corporation (RG&E) to promptly negotiate and file a Reliability Support Services Agreement (RSSA) for the continued operation of the Facility to support electric system reliability both on the bulk transmission system and in RG&E's service territory.

Historically, Ginna sold a majority of the Facility's output to RG&E under a purchase power agreement (PPA); but, that agreement expired on June 30, 2014. Since then, Ginna has operated as a merchant generator selling into the wholesale markets managed by the New York Independent System Operator, Inc. (NYISO). Ginna alleged in its Petition that revenues the Facility has earned in recent years have been insufficient to cover the costs of its operation, and will continue to be insufficient for the foreseeable future. On February 21, 2014, Ginna, RG&E, and the NYISO entered into a reliability study agreement resulting in the NYISO's production, on May 12, 2014, of the 2014 Reliability Study.³ The Reliability Study found that the retirement of Ginna would result in bulk transmission system and non-bulk local distribution system reliability violations in 2015 and 2018, the two years studied.

³ New York Independent System Operator, Additional Reliability Study for Exelon Corporation - Final Report, (May 12, 2014) (Reliability Study).

On November 14, 2014, the Commission issued an order finding a need for the continued operation of the Facility to ensure reliability.⁴ Based on such finding, the Commission directed RG&E to participate in negotiations with Ginna over an RSSA. On February 13, 2015, pursuant to the Commission's November Order, RG&E filed an RSSA. Simultaneously, Ginna filed the RSSA with the Federal Energy Regulatory Commission (FERC) resulting in the initiation of a parallel proceeding there.

On July 2, 2015, Administrative Law Judges Sean Mullany and Ashley Moreno conducted a temporary rates hearing that included the admission of testimony and exhibits into the record of this proceeding.⁵ Such exhibits are referenced herein.

Contemporaneous to the state proceedings, in accordance with FERC's establishment of settlement procedures, the parties negotiated at FERC in attempt to reach a complete settlement of all federal and state issues presented in this matter.⁶ After significant efforts, the parties reached a settlement in principle, and on October 21, 2015, RG&E filed the

⁴ Case 14-E-0270, Order Directing Negotiation of a Reliability Support Service Agreement and Making Related Findings, (issued November 14, 2014) p. 17, 24).

⁵ See, Case 14-E-0270, Evidentiary Hearing Transcript 7.2.15 Albany 1030, (issued July 21, 2015); see also, Ruling Admitting Exhibits, (issued July 31, 2015).

⁶ Pursuant to Commission regulations, RG&E filed in this matter a Notice of Impending Settlement Negotiations on May 5, 2015.

Joint Proposal.⁷ In addition to the supporting parties, other participants in the negotiations have chosen not to object to the settlement.⁸ Two other participating parties are objecting only in part.⁹

OVERVIEW OF THE JOINT PROPOSAL

The Joint Proposal (JP) satisfies the Commission's criteria and guidelines for settlements as established in its Opinion 92-2.¹⁰ Specifically, the settlement mitigates the impact of the RSSA on ratepayers, while striking a balance by recognizing the interests of investors in Ginna and preserving RG&E's long-term viability. The result of the settlement is consistent with prior Commission actions, consistent with FERC's legal parameters for accepting settlements, notwithstanding flaws in those parameters, and compares favorably to the

⁷ The signatories to the Joint Proposal are Ginna, RG&E, the Department of Public Service Staff, the Department of State Utility Intervention Unit, and Multiple Intervenors (collectively, supporting parties). FERC Staff participated in negotiations in an effort to resolve the parallel proceeding at FERC and is a signatory to the proposed settlement in FERC Docket ER15-1047-000.

⁸ The non-objecting parties are Entergy Nuclear FitzPatrick, LLC, Entergy Nuclear Indian Point 2, LLC, Entergy Nuclear Indian Point 3, LLC, and Entergy Nuclear Operations, Inc. (collectively, Entergy), and NRG Energy, Inc. (NRG).

⁹ The parties objecting in part are Alliance for a Green Economy (AGREE) and Citizens Environmental Coalition (CEC).

¹⁰ Cases 90-M-0255, et al., Procedures for Settlement and Stipulation Agreements, Opinion 92-2 (issued March 24, 1992), Appendix B at p. 8.

potential outcome of litigation. These elements are reviewed in detail below.

A. The Joint Proposal Compared to the Original RSSA

The JP modifies the RSSA that was filed with the Commission and FERC on May 14, 2015. Among the changes made, the JP recommends that the Commission adopt a two-year RSSA with procedures for negotiating a new RSSA should one be necessary, thereby modifying the original RSSA's three year term. The modified term addresses the ratepayers' concern that the original RSSA may have required them to pay unnecessary costs due to its length. Based upon the Reliability Study and RG&E's upgrading efforts described herein, the need for the continued service of the Facility could cease nearly a year before the original term of the RSSA expired.

The two-year term is designed to address the immediate reliability need, terminating at the initiation of an RG&E transmission system reliability project known as the Ginna Retirement Transmission Alternative (GRTA). However, to address the possibility that a reliability need might continue past the expiration of the RSSA's two-year term, the amended RSSA sets forth a process for determining if an alternative beyond the two years is necessary, and the terms under which such alternative would be implemented. The change to a two-year term potentially

saves ratepayers millions of dollars while still insuring reliability.

In addition to the foregoing modification, the JP resolves all the issues raised before the Commission, including the use of credits, the level of surcharges and the adequacy of RG&E's planning in preparing to meet the reliability need. The JP includes a payment structure that shifts more market risk to Ginna by reducing the fixed payment it receives while allowing it to retain a greater share of market revenues. This modification creates an incentive to operate the plant at full capacity such that Ginna might maximize its sales revenues. However, the JP both protects ratepayers and Ginna by confining its earnings within a set range, bounded by going forward costs and the full cost of service. Thus, while the modified payment structure gives Ginna reasonable assurances that its earnings will be sufficient to address the issues that led to the need for the RSSA, it also protects ratepayers by preventing any overearnings that would result in excessive or unreasonable returns for Ginna.

The JP recommends that the Commission authorize RG&E to implement a rate surcharge to recover \$2.25 million per month¹¹ from RG&E's customers effective January 1, 2016, or as

¹¹ The rate surcharge will replace the present temporary surcharge which recovers \$1.88 million per month.

soon thereafter as possible, to recover amounts paid to Ginna under the RSSA, with RG&E's obligation to make payments to Ginna commencing as of the effective date of the surcharge. The JP recommends that the surcharge remain in effect until either the termination of the RSSA, the termination of any extension to the Agreement, or the termination of any other reliability solution needed after the term of the RSSA.

In accordance with the JP, RG&E will use up to \$110 million of regulatory liabilities (customer credits) to offset any costs of the RSSA that exceed the amounts RG&E collects via the surcharge. The issue of applying some amount of customer credits to cover RSSA costs has been aggressively pursued by several parties in this matter as no provision for such was contained in the original RSSA.

The settlement terms resolve this issue by mitigating costs to RG&E's customers, while protecting RG&E's interests in maintaining credit quality through capping the recommended total amount applied of credits that can be applied to both the RSSA costs and rate increases, if any, in RG&E's pending rate case.¹² The latter is achieved through restrictions the supporting parties have agreed to on the use of credits in the rate

¹² Case 15-E-0285, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Rochester Gas and Electric Corporation for Electric Service, (filed May 20, 2015).

proceeding. Thus, the use of customer credits as applied to the one-time RSSA costs is appropriate in that it reduces the financial burden of the RSSA on customers, but seeks to prevent any negative impact on RG&E's credit quality ratings. As a result, a downgrade of RGE's credit rating is avoided, concomitantly avoiding adverse impacts to utility shareholders that would also redound to the detriment of customers through the increased costs attendant to borrowing both short and long term capital at less favorable terms than would be obtained at the existing credit rating.

ELEMENTS OF THE JOINT PROPOSAL

A. Payments to Ginna

Under the JP, RG&E is obligated to pay Ginna a fixed payment of \$15.420 million per month during the 24 month term of the RSSA. Additionally, Ginna will retain 30% of all energy and capacity market revenues, while 70% of such revenues and 100% of ancillary services revenues will be credited to RG&E as an offset to the monthly fixed payments due to Ginna. Finally, RG&E will pay Ginna a one-time Settlement Payment of \$11.458 million following the expiration of the RSSA.

Ginna's total compensation during the term of the RSSA will be subject to a \$425 million "floor" set at negotiated going forward costs (GFC) and a \$510 million "cap" set at the negotiated full cost of service (FCOS). The combined payments

made by RG&E together with 30% of market revenues shared with Ginna during the RSSA's term will be reconciled to the above floor/cap amounts calculated over the term of the RSSA. The reconciliation would occur within three months of March 31, 2017, and would follow reductions to the "floor" and the "cap," dollar-for-dollar, for any Performance Adjustments assessed pursuant to paragraph 5.3 of the RSSA. These adjustments are intended to insure that Ginna provides satisfactory service and will reduce Ginna's compensation should the Facility not operate as intended under the RSSA.

The table below shows Ginna's expected compensation ranges based on current energy and capacity market prices. To trigger the floor on Ginna's compensation, market revenues would have to fall to \$15.06/MWh,¹³ and to reach the cap, market prices would have to increase to \$44.50/MWh. Staff forecasts that market prices will not cause Ginna's compensation to fall below the floor and does not, therefore, expect any additional amounts will be due to Ginna at the end of the RSSA. On the other hand, if market prices rise to the higher levels seen historically

¹³ If electric prices fall to these levels, electric commodity costs for customers will also fall. The reduction in commodity costs would offset some or all of the related increases in Ginna RSS costs.

prior to the more recent overall fall in prices, Ginna may be providing credits to ratepayers.

RSSA Estimated Compensation with Cap and Floor

<u>\$ Millions</u>		<u>RSSA</u>	<u>Cap</u>	<u>Floor</u>
Fixed	\$15.4/month	\$370.1	\$370.1	\$370.1
Market Revenues	30%	\$92.9*	\$128.5	\$43.5
Settlement Payment	\$11.5	<u>\$11.5</u>	<u>\$11.5</u>	<u>\$11.5</u>
Total		<u>\$474.5</u>	<u>\$510.0</u>	<u>\$425.0</u>
\$/MWh		\$49.32	\$53.01	\$44.17

*Estimated based on October 20, 2015 prices.

In its Order in the parallel federal proceeding, FERC indicated a need for a cap and floor on the RSSA payments.¹⁴

FERC stated,

"[W]e provide the following guidance. Regarding the RSSA rates, in the NYISO RMR Order, the [FERC] stated that "[c]ompensation to an RMR generator must at a minimum allow for the recovery of the generator's going-forward costs, with parties having the flexibility to negotiate a cost-based rate up to the generator's full cost of service." Consistent with that policy...the presiding judge should ensure that a record is established to support that the RSSA rates are not lower than the level required to recover Ginna's going-forward costs, but not higher than the level required to recover its full cost of service.¹⁵

¹⁴ F.E.R.C. Docket ER15-1047-000, R.E. Ginna Nuclear Power Plant, LLC, Order Rejecting in Part, and Accepting in Part and Suspending Proposed Rate Schedule, Subject to Refund, and Establishing Hearing and Settlement Procedures, (issued April 14, 2015) p. 21 (FERC Ginna Order).

¹⁵ Id. at ¶43.

Notwithstanding flaws in FERC's approach, discussed further below, Staff evaluated Ginna's estimated cost of service, both on a fully embedded basis (FCOS) and on a going forward basis (GFC), arriving at estimates of \$514.5 million for FCOS and \$402.1 million for GFC, respectively. The FCOS in the JP is set at \$4.5 million lower than Staff's estimate, while the GFC is \$22.5 higher.

1. Staff's Review of Going Forward Cost (the "floor").

Even though the imputed GFC number in the JP is slightly higher than Staff's estimate, that level is reasonable. Nuclear plants are exposed to potential risks and costs, such as safety, emergency preparedness, and employment of expensive specialized personnel that should be taken into account when determining the reasonableness of compensation. Assumptions made in arriving at the value of these risks and costs affect the forecast of GFC. Moreover, for Ginna's compensation to reach the floor, market prices would have to decline to previously unseen levels, below \$15.06/MWh, on a sustained basis.

2. Staff's Review of Full Cost of Service (the "cap").

In order to arrive at the estimated \$514.5 million FCOS, Staff began with Ginna's FCOS before Ginna's recent mark

down of fair market value,¹⁶ which occurred when Ginna's plant and related assets were essentially written off (impaired) in December 31, 2014 due to its loss of economic value caused by low market prices. In developing Ginna's FCOS in the settlement, Staff continued to reflect plant balances (return and depreciation) at levels that preceded the write down. Although Staff acceded to the inclusion of these costs even though FERC might have rejected them, the result is that Ginna accepted, in settlement, a FCOS that is lower than Staff's overall estimate.

Staff made several ratemaking adjustments that reduce Ginna's pre-write down FCOS. First, it removed the nuclear waste fee paid to the United States Department of Energy (DOE) since the DOE stopped collecting the fee in 2014.¹⁷ Next, Staff

¹⁶ See, F.E.R.C. Docket ER15-1047-000, R.E. Ginna Nuclear Power Plant, LLC, Prepared Direct Testimony of Alan C. Heintz, p. 16-18 (GIN-600).

¹⁷ The nuclear waste fee was established under the Nuclear Waste Policy Act of 1982 to fund the disposal of utility spent nuclear fuel. In return, the DOE was supposed to begin disposing of that used fuel by January 31, 1998. The DOE has not yet disposed of any utility spent fuel, and in 2010 it dismantled the congressionally mandated repository program at Yucca Mountain, Nevada. The National Association of Regulatory Utility Commissioners and Nuclear Energy Institute sued DOE in the US Court of Appeals for the District of Columbia Circuit in 2011 after the department refused to suspend the collection of the fee. The court in November ordered the DOE to suspend collection of the fee until the Yucca Mountain program is restarted or Congress takes legislative action to establish a new spent fuel program.

adjusted the allocation of corporate overheads from an allocator based on salaries and wages to an allocator that is more consistent with historical approaches used by Ginna's parent. Staff also removed the accelerated depreciation impacts from Ginna's cost of service, since there is no basis for recovering Ginna's investments from RG&E's customers via accelerated depreciation. Fuel costs were also adjusted to remove the effect of compression and to more accurately reflect costs based on Ginna's output. Finally, Staff reduced Ginna's cost of capital to more accurately reflect its new status as a provider of regulated reliability service instead of a competitive market participant. Thus, we provided a return on capital at a level more in-line with that of a regulated utility. Staff reduced Ginna's return on equity (ROE) from 10.7% to 9.0% and Ginna's equity ratio from 55% to 48%.

Working from the FCOS, Staff then made the following additional adjustments to arrive at GFC. First, Staff removed all sunk costs, including all remaining return on investment and depreciation. Then, Staff added back to GFC \$40 million in estimated capital expenditures for Ginna, a portion of which are subject to a claw-back in the event that Ginna continues to operate beyond the term of the RSSA.¹⁸

¹⁸ The projected capital expenditures reflect lower levels than historical capital expenditures.

The following table summarizes the adjustments to FCOS and GFC.

**Ginna Cost of Service and Going Forward Costs
Staff Estimates
\$ Millions**

# months	<u>9</u>	<u>12</u>	<u>3</u>	<u>24</u>
	2015	2016	2017	Sum
Filed Cost of Service (COS)	\$ 286.1	\$ 346.9	\$ 92.9	\$ 725.9
\$/MWh	\$ 84.4	\$ 69.5	\$ 74.9	\$ 75.4
Settlement Adjustments - COS	\$(64.0)	\$(125.4)	\$(22.0)	\$(211.4)
Ginna COS	\$ 222.1	\$ 221.5	\$ 70.9	\$ 514.5
\$/MWh	\$65.5	\$44.4	\$57.1	\$53.5
Settlement Adjustments - GFC	\$ (41.4)	\$ (60.7)	\$ (10.3)	\$(112.4)
Going Forward Costs	<u>\$ 180.7</u>	<u>\$ 160.8</u>	<u>\$ 60.6</u>	<u>\$ 402.1</u>
\$/MWh	\$53.3	\$32.2	\$48.9	\$41.8
Total Adjustments	<u>\$(105.4)</u>	<u>\$(186.1)</u>	<u>\$(32.3)</u>	<u>\$(323.8)</u>
MWh	3,388.9	4,992.3	1,240.4	9,621.6

Based on Staff's evaluation of the FCOS and GFC, the cap and floor amounts in the settlement are reasonable given the uncertainties of litigated outcome for Staff's adjustments.

3. Revenue Structure is Just and Reasonable.

The payment structure detailed above is reasonable. Pursuant to FERC standards,¹⁹ GFC and FCOS represent, respectively, thresholds for a floor and cap. While FERC

¹⁹ See, FERC Ginna Order at 21, ¶ 43, citing, New York Indep. Sys. Operator, Inc., 150 FERC ¶61,116, at P 17 (2015).

misapplied the law in arriving at its standards, when reviewed under properly applied standards, the outcome remains reasonable.

FERC recently instructed the NYISO that RMR compensation "must at a minimum allow for the recovery" of a generator's GFC, but permitted negotiation of a higher rate up to the full COS.²⁰ The alternative of setting RMR compensation at a rate up to the full generator's COS, however, would result in rates that are unjust and unreasonable. The U.S. Constitution does not require that an uneconomic generator seeking to retire be paid its COS for reliability services provided, rendering a rate based on GFC constitutionally adequate.

In Market Street Railway, the U.S. Supreme Court considered the compensation that a utility whose operations have become uneconomic because of market forces must be provided in order to pass Constitutional muster.²¹ Reviewing and distinguishing prior precedent, the Court explained that those decisions do not ensure that regulated businesses facing their demise because of economic forces must earn a profit. The Court

²⁰ RMR Order at ¶17. See also Ginna Order at ¶43 (instructing that RMR compensation at a minimum must cover only a generator's GFCs).

²¹ Market St. Ry. Co. v. R.R. Comm'n of California, 324 U.S. 548 (1945).

explained that the due process clause cannot "be applied to insure values or to restore values that have been lost by the operation of economic forces."²² A company engaged in public service "cannot be said to suffer injury" if it receives a rate for a temporary period "which probably will produce a fair return on the present fair value of their property."²³

Significantly, the D.C. Circuit Court of Appeals overturned a rate decision made by the Washington Metropolitan Area Transit Commission (Transit) because it ignored Market Street Railway.²⁴ Speaking directly to the circumstances here, Transit had approved a rate that guaranteed a return in exchange for a public service that was uneconomic.

The settlement arrived at here, however, meets the Market Street Railway test. It sets a GFC floor, properly recognizing the costs Ginna will incur by remaining in service even though it is no longer economically viable. While payments to Ginna cannot fall below the floor, under the JP, Ginna shares in the risks and benefits of wholesale electric markets, which is appropriate under these circumstances where Ginna can

²² Id at 566-67.

²³ Id. It is indisputable that a generator needed for reliable transmission system operation is providing an essential public service. A contrary finding would eviscerate the entire justification for RMR agreements.

²⁴ Democratic Central Committee of the Dist. of Columbia v. Washington Metropolitan Area Transit Comm'n, 485 F.2d 886 (D.C. Cir. 1973).

continue to access substantial revenues though those markets but nonetheless plans to abandon service. As a result, any revenues it might earn above the floor are justified notwithstanding the abandonment. Since the rate is not tied to COS in any way other than through the cap, use of that standard -- constitutionally inappropriate in an abandonment setting -- does not harm RG&E customers and instead offers those customers some protection from the market risk they share with Ginna.

B. Use of Customer Credits

Since RG&E's payments to Ginna under the RSSA will not commence until both FERC and the Commission approve of the RSSA and/or authorize recovery of payments by RG&E, the monies owed to Ginna retroactive to April 1, 2015 will be paid to Ginna over the remaining term of the RSSA (i.e., through March 2017). These payments are referred to as the Deferred Collection Amount and will include carrying costs at the Other Customer Capital Rate, which is currently 2.9%.

The JP provides that RG&E will implement an increase in the surcharge raising it to \$2.25 million per month effective January 1, 2016, to recover amounts paid to Ginna under the RSSA (the RSSA surcharge).²⁵ Staff estimates that RG&E will collect \$33.8 million from the RSSA surcharge between January 1, 2016 -

²⁵ The RSSA surcharge will include certain other amounts identified in this settlement as being recovered through the rate surcharge.

March 31, 2017. Due to low projected wholesale market electric prices, Staff expects that the RSSA surcharge will continue until October 2017 in order to fully collect the amounts due Ginna. During that latter period, the RSSA surcharge will collect approximately \$15.4 million for a total collection of \$49.2 million.

To mitigate bill impacts, the JP requires RG&E to use deferred rate credit amounts (regulatory liabilities) to offset the full amount of the Deferred Collection Amount retroactive to April 1, 2015 (including carrying costs), and all RSSA cost amounts owed Ginna that exceed the \$2.25 million per month surcharge. As a concession to RG&E's credit quality and cash flow concerns, the JP also provides, however, that the total amount of credits used to offset RSSA costs will not exceed \$110 million through March 31, 2017. Staff believes this outcome is beneficial to all involved and was even suggested by the Commission when, in setting temporary rates, it "agree[d] that use of the credits to offset a significant portion of the RSSA costs is a wise course of action."²⁶

Upon implementation of the RSSA surcharge, customer's bills will increase to reflect the new surcharge level. To the extent that the RSSA costs exceed the \$2.25 million/month

²⁶ Case 14-E-0270, Order Approving Establishment of Temporary Rates, (issued August 14, 2015) p. 17 (the Temporary Rates Order).

surcharge, the amount of the RSSA costs will then be mitigated through the use of customer credits. The amount of credits used to offset RSSA costs can be estimated based on current market prices.

To estimate the amount of the credits that would be used, Staff added the Deferred Collection Amount to the stream of monthly fixed payments due Ginna, and then subtracted the sum of 70% of Ginna's expected market revenues and the amounts slated for collection through the temporary surcharge commencing January 1, 2016. The table below presents the current estimate of the cost of the RSSA:

**Net Cost to Customers
Over The Collection Period of the RSSA
\$ Millions**

<u>Component</u>	<u>Total</u>
Fixed Payments	\$370.1
Settlement Payment	\$11.5
Total Payments to Ginna	381.6
Less: 70% Market Revenues	(214.9)
Less: RSSA Surcharge	(49.2)
Less: Temporary Surcharge	(7.5)
Total Offsets	(271.6)
Net Cost to Customers to be Offset with Customer Credits	\$110.0

*Estimated based on October 20, 2015 prices.

The increase paid to Ginna above the temporary surcharge level was arrived at as a component of an overall settlement package that included a substantial use of one-time credits, a shifting of more market risk to Ginna, and a cap on Ginna's compensation. The resulting bill impacts, after mitigation by one-time credits, will produce a bill increase of 2.4% on average or 0.3% over the current Temporary Rate Surcharge, while maintaining adequate cash flow to RG&E. As a result, RG&E's credit rating will remain robust, enabling it to continue accessing capital at reasonable costs.

1. Use of Customer Credits Mitigates Bill Impacts

In the recent Temporary Rates Order, opposing parties argued that RG&E has approximately \$155 million in regulatory liabilities, or customer credits, on its books that should be applied to offset all costs arising from the RSSA.²⁷ Staff has reviewed the amount of credits available to RG&E, as the amounts of credits shown in Exhibit 6 here differ from amounts shown in the pending RG&E rate case.²⁸ After its review, Staff believes that there are sufficient credits to offset the RSSA costs while

²⁷ See, case 14-E-0270, Order Approving Establishment of Temporary Rates, (issued August 14, 2015), p. 3-4, citing, Hearing Exhibit 6, Discovery Request Response of RG&E to Multiple Intervenors (MI 39) Request No. GNP-15-092 (April 9, 2015) (Exhibit 6).

²⁸ See, Case 15-E-0285, Staff Accounting and Tax Panel, Exhibit____(SAT-2), Schedule C, Deferred Debit and Credits.

retaining a balance for use in the pending and future rate cases.

First, the amounts in Exhibit 6 reflect only that subset of the total customer credits available, that appear in RG&E's 2009 rate plan annual compliance filing (ACF) for 2014. Exhibit 6 omits certain other customer credits that are not reflected in the company's ACF but are recorded elsewhere, while the rate case exhibit shows all amounts owed to customers. Second, the amounts in Exhibit 6 represent actual credit balances, including interest, as of December 31, 2014. The amounts shown in the rate case are a forecast of such amounts as they change over time through the end of the rate year in March 2017 that is proposed in the rate case.

RG&E's pending electric rate case exhibit is a more accurate source of the amount of credits. The forecast rate case amounts incorporate known and expected changes in all credit and debit balances from 2014 through the rate year ending March 31, 2017.

The rate case exhibits show RGE's residual amount of net deferred credits to be \$113.7 million.²⁹ However, this rate case estimate includes \$168.6 million in offsets for tax deferrals that have not been approved by the Commission. Staff

²⁹ See, Case 15-E-0285, Staff Accounting and Tax Panel, Exhibit____(SAT-2), Schedule C, Deferred Debit and Credits.

removed these unapproved offsets. Also, the \$113.7 figure does not include \$9.7 million in Beebee and Russell decommissioning costs that RG&E should recover from ratepayers. After excluding these tax deferrals and including the decommissioning costs, Staff finds there are \$272.6 million of credits available, \$117.3 million more than the \$155.3 million in Exhibit 6.

Based on recent wholesale electric market price information and the terms of the settlement agreement, Staff estimates that \$110 million of rate credits will be utilized during the term of the RSSA to mitigate bill impacts. The remainder is a sufficient resource for use in RG&E's pending rate case. As noted in the Temporary Rates Order, use of one-time credits to offset one-time costs is good ratemaking practice, avoiding the distortion that can occur in rates if one-time credits are applied to on-going costs. Moreover, we are mindful of the equity arguments urging us to return the credits as closely as possible in time to the same ratepayers on whose behalf they accrued. Nevertheless, we are also sensitive to the fact that the use of all regulatory liabilities at one time could have a negative impact on RG&E's cash flow.³⁰ Finally, although the JP limits its parties from seeking to use more than \$10 million in credits during the proposed rate year ending March 2017, such condition is part of a total package

³⁰ Temporary Rates Order, p. 17-18.

that was negotiated among the parties to balance the parties' interests in maintaining reasonable rates while providing adequate cash flow to RG&E.

2. Limits on Use of Customer Credits and Cash Flow

The limits on the use of one-time credits were negotiated to balance the parties' interests in maintaining reasonable rates while maintaining adequate cash flow. In RG&E's current rate case, it has presented calculations of relevant financial ratios for the Rate Year from both Moody's and S&P.³¹ Three of Moody's ratios justify an 'A' rating while the other equates to a 'Baa' rating. Both of S&P's core ratios equate to an 'A- / BBB+' rating. Additionally, three of the five supplemental ratios are between 'BBB' and 'A- / BBB+.' The RG&E Policy Panel indicates that Moody's and S&P would likely assess the Companies' credit quality at a 'BBB' to 'A-' credit rating for both NYSEG and RG&E.³² While the \$66.6 million reduction in cash flows from use of the credits will likely negatively impact the Companies' credit metrics to some extent, they will remain in the middle- / BBB+ category. A decline in credit metrics at that level, however, should not adversely affect RG&E's credit ratings. Moreover, the use of credits here is a one-time event. The rating agencies tend to look at longer

³¹ Prepared Testimony of RG&E's Policy Panel, Exhibit____(RRP-8).

³² See id.

term impacts and will likely focus on the results of the upcoming rate case in assessing RG&E's credit.

In order to protect from excessive debt leverage caused by reduced cash flow, the JP provides that RG&E will not make dividend payments until its equity ratio is sufficiently above its minimum equity requirement, which is currently 48%. The purpose is to ensure that the amount of any dividend payment will not cause the equity ratios to fall below the minimum equity level. RG&E's parents, however, will not be required to make equity infusions during the term of the RSSA, which is a reasonable protection for its ultimate shareholders.

This aspect of the JP highlights and strengthens the minimum equity ratio requirement imposed in the recent Iberdrola restructuring order.³³ Under such Order, RG&E must maintain a minimum equity ratio of no less than 300 basis points below the equity ratio used to set rates. In the event that NYSEG, RG&E, or parent ratings are downgraded to the lowest investment grade with a negative watch, or ratings are downgraded to non-investment grade, RG&E is prohibited from issuing dividends that would result in a trailing 13-month average common equity less than the maximum equity ratio, exclusive of goodwill, utilized for the Companies' earnings sharing mechanism. Also, under

³³ See, Case 12-M-0066, Iberdrola USA, Inc., Order Adopting Staff Report and Approving Reorganization, (issued November 5, 2013).

these circumstances, RG&E must maintain a minimum equity ratio, exclusive of goodwill, of no less than the equity ratio used to set rates. The minimum equity ratio requirement ensures that the companies are not over leveraged, and the JP fits within that framework.

C. Commission Precedent

The Ginna RSSA was preceded by both the Dunkirk and Cayuga RSS Orders.³⁴ In both the Dunkirk and Cayuga cases, the Commission provided guidance on the appropriate level of compensation for an RSSA. Ginna is distinguishable, however, from those prior cases in that the operators of both Dunkirk and Cayuga were considering temporary shut downs (mothballing) while here Ginna effectively provided notice for a permanent retirement. The main distinction between mothballing a plant and permanent retirement is that when mothballing, depreciation may not be considered as an avoidable cost since continued operation could create additional wear and tear on physical assets that could in theory at least return to service in the

³⁴ See, Cases 12-E-0136, Petition of Dunkirk Power LLC and NRG Energy, Inc. for Waiver of Generator Retirement Requirements, Order Deciding Reliability Issues and Addressing Cost Allocation and Recovery, (issued August 16, 2012); see also, Case 12-E-0400, Petition of Cayuga Operating Company, LLC to Mothball Generating Units 1 and 2, Order Providing for Cost Review and Recovery and Making Other Findings, (issued December 12, 2014).

future. In a retirement situation, the owner of the assets concedes they are essentially worthless for future use.

Staff notes that there are many common features among the Cayuga, Dunkirk, and Ginna RSSAs providing the Commission with an opportunity to maintain a consistent approach in approving such agreements. The payments under the RSSAs all fall within a range between FCOS and GFC. The payments generally include property taxes and overheads, but exclude most sunk costs, while Cayuga's RSSA includes capital expenditures, subject to a partial claw back if the units continue to operate post-RSSA. They also all include revenue sharing and performance penalties.

It is difficult to precisely compare each of the RSSAs due to the types of plants and the shutdown approaches. The largest difference is that compared to Cayuga and Dunkirk which are coal units and run when needed for reliability or in the event that economic conditions dictate, Ginna is a nuclear plant which is generally a baseload unit (i.e., output is not varied to track economic conditions). As a result, the approach to revenue sharing is different, with Ginna sharing 70% of energy and capacity revenues with customers. In Cayuga and Dunkirk, 100% of capacity revenues are credited to customers, while these plants retain up to 100% of net energy revenues (in Cayuga net energy revenues are shared 50/50 above \$5 million).

Since Ginna cannot alter its output based on economic conditions, and ratepayers benefit by the revenue offset provided through revenue sharing, the parties agreed that ratepayers should receive the majority of revenues. However, the parties also agreed that Ginna should have a powerful incentive to operate at maximum output so that revenues would be maximized.

As a result, the JP reflects an increase in Ginna revenue sharing from 15% to 30%. This increase in sharing places more of Ginna's compensation at risk; from market prices and from Ginna's output. The increase in Ginna's sharing was accompanied by a reduction in Ginna's monthly fixed payment; thus Ginna's overall compensation was not increased. Therefore, the terms of the Ginna RSSA are reasonable considering the facts and circumstances, and are consistent with Commission precedent.

RELIABILITY

The NYISO indicated, in its Reliability Study of May 12, 2014,³⁵ that retirement or mothballing of Ginna would result in bulk transmission system and non-bulk local system reliability violations in 2015 and 2018, the two years studied. Utilities are required to meet the reliability design criteria the NYISO used based upon anticipated electric loads, power

³⁵ New York Independent System Operator, Additional Reliability Study for Exelon Corporation - Final Report, (May 12, 2014) (Reliability Study).

system configurations and facilities in service. These rules and standards are designated and defined nationally by the North American Electric Reliability Corporation (NERC), regionally in the Northeast by the Northeast Power Coordinating Council (NPCC), and statewide in New York by the New York State Reliability Council (NYSRC). The criteria are specified in terms of having the capability to adequately serve loads: (a) without thermally overloading power system equipment (i.e., avoiding subjecting equipment to damaging over-heating); and (b) while maintaining voltage levels within an acceptable range without experiencing sustained high or low voltage excursions, either of which may result in damage to utility or customer equipment and in extreme cases may cause a widespread blackout. Failure to adhere to these criteria may result in serious operational and safety consequences, as well as significant financial penalties for RG&E.

In the study years of 2015 and 2018 no thermal or voltage reliability criteria violations were shown to occur on the 115 kV and above power system in the Rochester area with Ginna in service. However, without Ginna in service, thermal overloads would occur on the 345/115 kV transformers at the Pannell (Station 122) Substation in the Rochester area during peak periods for both 2015 and 2018. These overloads would necessitate load shedding, although the overloads would be

somewhat less severe in 2018 compared to 2015 presumably due to the assumed entry into service of the Rochester Area Reliability Project (RARP). Thus, no reliability violations are expected on the 115 kV system and above in the Rochester area with Ginna in service, but thermal reliability violations would occur during peak periods without Ginna in service.

Importantly, if Ginna were absent, the outage loss of one 345/115 kV transformer at the Pannell Station 122, would overload the other two remaining 345/115 kV transformers there. To the extent that the initial transformer outage at Pannell involved severe and permanent damage to that transformer, the remaining system facilities would be inadequate in serving peak loads, potentially for several weeks before equipment repairs or replacements could be completed.

To address the reliability violations in the Rochester Area, without a continuing need for Ginna, RG&E proposed the Ginna Retirement Transmission Alternative (GRTA) which is expected to be in service by June 2017. The work would consist of (a) replacement of three 345/115 kV transformers at Pannell Station 122 with larger transformers; (b) 345 kV bus reconfiguration to a breaker and a half scheme there; and (c) upgrades to 34.5 kV and 11.5 kV circuits. Additionally, 345 kV work will be completed at Rochester Station 80 to eliminate reliability criteria violations resulting from stuck breaker

contingencies. Staff concurs that this proposed work will appropriately strengthen the Rochester area power system and will address reliability issues currently anticipated to result from a shutdown of Ginna.

Until the GRTA project is completed, the Ginna RSSA Settlement Agreement provides for continued reliable operation to prevent reliability criteria violations, and to avoid customer load shedding under generally anticipated conditions. Importantly, in comparison to the original RSSA, the Ginna RSSA Settlement Agreement provides for a permanent reliability solution to the shutdown of Ginna. It helps ensure the GRTA will either resolve any outstanding reliability issues, or an alternative is in place to satisfy the reliability needs.

Specifically, the revised RSSA requires RG&E, in coordination with the NYISO, to perform an updated reliability study to confirm that reliability issues continue to exist, and that the GRTA as proposed or as subsequently modified by the study will resolve any reliability needs resulting from a retirement of Ginna. Second, if the study finds that the GRTA fails to address all reliability needs, the RSSA requires RG&E to issue a solicitation for alternative solutions. According to the RSSA, Ginna must participate in the solicitation if one is issued. Lastly, the RSSA provides additional oversight for the

GRTA by requiring RG&E to issue periodic progress reports and hold monthly meetings on the status of the project.

CONCLUSION

The terms of the Joint Proposal fully satisfy the Commission's Settlement Guidelines. Taken as a whole, the Commission can reasonably conclude that the terms of the Joint Proposal would fall within the range of potential results of litigation. As noted above, the fact that five active parties have signed on to the Joint Proposal is testament to the breadth of agreement on a wide range of issues and balancing of the interests of customers, RG&E, Ginna and the other Parties. The Joint Proposal significantly continues and advances the Commission's goals and policies, including maintaining reliability while limiting the impacts of the costs of the RSSA during the term of the proposed RSSA. RG&E, meanwhile, will receive sufficient funds to operate and manage its electric, business, and maintain safe and adequate service. For all of the above reasons, Staff respectfully recommends that the terms of the Joint Proposal be found to be in the public interest and that they be adopted by the Commission in their entirety.

Respectfully submitted,

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Albany, New York