SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
Docket No. A-002518-20

In the Matter of the Application of PSEG Nuclear, LLC and Exelon Generation Company, LLC for the Zero Emission Certificate Program – Salem Unit 1	)	APPELLATE DIVISION **Docket No. A-002518-20** Civil Action
In the Matter of the Application of PSEG Nuclear, LLC and Exelon Generation Company, LLC for the Zero Emission Certificate Program – Salem Unit 2	)	On Appeal from Orders of the New Jersey Board of Public Utilities in: Docket Nos. ER20080557, ER20080558, ER20080559
In the Matter of the Application of PSEG Nuclear, LLC for the Zero Emission Certificate Program – Hope Creek	)	

REPLY BRIEF OF APPELLANT NEW JERSEY DIVISION OF RATE COUNSEL

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PRELIMINARY STATEMENT

In the three Orders below, the New Jersey Board of Public Utilities ("BPU" or "Board") awarded approximately $800 million in ratepayer-funded subsidies in the form of Zero Emissions Certificates ("ZECs") to three unregulated nuclear generating units owned and operated by the applicants, PSEG Nuclear, LLC ("PSEG Nuclear") and Exelon Generation Company, LLC ("Exelon"), for a second three-year eligibility period. Subject to only limited "recapture" provisions, the unit owners will collect these subsidies whether or not the units prove to be more profitable than indicated by the financial projections they submitted to the Board.

The briefs filed by the Respondents BPU, PSEG Nuclear, and Exelon attempt to suggest that the Orders below were based on an abundance of credible evidence that was thoroughly analyzed by the Board and that the challenges to that evidence asserted by Appellant the New Jersey Division of Rate Counsel ("Rate Counsel") and others are largely precluded by the legislation that authorized the subsidies and an earlier decision of this Court. This is not the case. PSEG Nuclear, which operates all three units, submitted financial projections which the company itself recognized overstated the amount of subsidies that were needed for the units to continue operation, thus raising a fundamental issue of credibility. Further, Rate Counsel and

Respondent the Independent Market Monitor ("IMM") for PJM presented evidence of several specific flaws in the applicants' projections of costs and revenues. In the Orders below, the Board acknowledged that this evidence raised issues of fact concerning the applicants' quantifications of both their projected costs and their projected revenues. However, instead of affording reasoned consideration to these issues, the Board simply dismissed the evidence opposing subsidies in a few conclusory statements.

Contrary to the Respondents' arguments, the Board's Orders do not reflect a thorough weighing of evidence on disputed factual issues that is a fundamental requirement of administrative decisionmaking. While the three Board Orders catalogued the evidence and positions of the parties, they did not reflect that the Board weighed the evidence as to each of the key disputed factual issues before it.

Nor were the results of the Board's analysis dictated by the enabling statute, or this Court's affirmance of the Board's decision in the first ZEC proceeding. Unlike the first ZEC proceeding, where this Court found that the Board had no authority to consider ZEC subsidies below the statutory maximum, the proceedings below were subject to a statutory provision that specifically charged the Board with ensuring the affordability of the ZEC charges by lowering the ZEC charge to the minimum

needed to keep the plants open. This provision gave the Board the authority, and the duty, to critically examine financial projections presented by the applicants to quantify the subsidies claimed to be needed. The Board did not do this.

In the end, it is apparent that the Board's decision was based not on a careful examination of the evidence but on the applicants' threat to close all three units unless they all received the maximum subsidy of $10 per megawatt hour. As one of the Board's Commissioners stated, the applicants received the statutory maximum subsidy because of their "intransigence" in demanding the full amount. (Aa389)[1] While the Board was understandably concerned that the nuclear units would shut down, it was obligated to determine how much subsidy was actually needed, based on an objective analysis of the evidence, and not simply accede to the unit owners' demands for maximum amount. Because the three Board Orders below do not reflect such analysis, they must be reversed as arbitrary and capricious.

STATEMENT OF FACTS AND PROCEDURAL HISTORY

[1] Rate Counsel's initial brief in this matter will be cited herein as "Ab___), The public and confidential volumes of Rate Counsel's appendix will be cited, respectively as "Aa___" and "Aca___." The brief of respondent BPU will be cited as "BPUb___." PSEG Nuclear's brief and Confidential appendix will be cited as "PSb__" and "PSca___", and Exelon's brief will be cited as "EXb__"). The transcript of the public portion of the evidentiary hearings before the Board on March 8, 2021 will be cited as "T__-__".

Rate Counsel relies on the Statement of Facts and Procedural History set forth in its initial brief.

ARGUMENT

POINT I

THE BOARD'S BLANKET REJECTION OF THE SUBSTANTIAL EVIDENCE OPPOSING THE APPLICANTS' SUBSIDY REQUESTS MUST BE REVERSED AS ARBITRARY AND CAPRICIOUS

In considering the challenges to the Orders below, it is important to recognize the legal and factual differences that distinguish this matter from the proceedings in which the Board initially awarded ZECs to three nuclear generating units. In the first ZEC proceeding, the Board was charged only with determining whether the units met the statutory criteria under N.J.S.A. 48:3-87.3 et seq. (the "ZEC Act") for receiving ZECs. The Board and this Court both determined that the Board had no authority to consider reducing the ZEC charges imposed on ratepayers below the statutory maximum of 0.4 cents per kilowatt hour. In re Implementation of L. 2018, C. 16 Regarding the Establishment of a Zero Emission Certificate Program for Eligible Nuclear Power Plants, 467 N.J. Super. 154, 185-87 (App. Div.), certif. denied 247 N.J. 414 (2021) (referred to hereinafter as the "ZEC I Affirmance").

In this proceeding, the Board was required to make an additional determination, governed by the following provision:

> Notwithstanding the provisions of paragraph (1) of this subsection, and to ensure that the ZEC program remains affordable to New Jersey retail distribution customers, the board may, in its discretion, reduce the per kilowatt-hour charge imposed by paragraph (1) of this subsection starting in the second three year eligibility period and for each subsequent three year eligibility period thereafter, provided that the board determines that a reduced charge will nonetheless be sufficient to achieve the State's air quality and other environmental objectives by preventing the retirement of the nuclear power plants that meet the eligibility criteria established pursuant to subsections d. and e. of this section.
>
> N.J.S.A. 48:3-87.5(j)(3)(a).

This provision requires the Board assure affordability for ratepayers by determining what level of subsidies is actually needed to prevent the nuclear units from retiring. Thus, in contrast to the first ZEC proceeding, where the only issue was whether the criteria for awarding ZECs were met, the proceedings below should have included a determination of exactly what subsidy levels were required.

While the above-quoted provision entrusts the decision to lower the ZEC charge to the Board's discretion, an administrative agency may not exercise its discretion in an arbitrary manner. The Board's exercise of its discretionary authority, like all of its determinations, must be based on substantial evidence in the record, and must be explained in a way that permits judicial review. Administrative agency discretion is "not unbounded and must be exercised in a matter

that will facilitate judicial review." Noble Oil Co. v. Dept. of Envt'l Prot., 123 N.J. 474, 476 (1991). An agency "must articulate the standards and principles that govern their discretionary decisions in as much detail as possible." Id. at 476-77, quoting Van Holten Group v. Elizabethtown Water Co., 121 N.J. 48, 67 (1990).

The second ZEC proceeding involved a new factual record. The applicants filed new applications, with new projections of costs, and new projected revenues based on different market conditions. Moreover, these new applications presented a circumstance that was entirely absent from the record of the first ZEC proceeding — the applicants' financial projections purported to show that they needed subsidies substantially in excess of the amount they were in fact willing to accept. (See Ab13, Ab23-24, Ab28-29, Ab35-36) This made it clear that the applicants' financial projections did not reflect actual need.

The sizeable discrepancy between the applicant's financial projections and the subsidy they actually sought should have led the Board to a careful analysis of how costs and revenues were quantified. Indeed, in the three Orders below the Board itself acknowledged that there were genuine factual disputes about "amount of costs, including the costs of risks, and revenues that the applicants will receive in the future." (Aa443, Aa509-10, Aa576) Nevertheless, the Board did not explain how it

weighed the evidence on those issues of fact. Instead, the Board simply stated that it was awarding subsidies based on its "review of the 'financial and other confidential information' submitted throughout this proceeding," and that it was declining to reduce the subsidy below the statutory maximum because it was "not persuaded" that it should do so. (Aa443, Aa510, Aa576)

The Board's statements beg the questions of why the Board determined that the statutory criteria had been met, and why it was "not persuaded" a lower subsidy would suffice. It is impossible to discern from the Board Orders which, if any, of Rate Counsel's and the IMM's suggested adjustments were given serious consideration. The Board's statement that it undertook a "careful and thorough review of the administrative record" (Aa441, Aa508, Aa574), is not a sufficient explanation of how the Board weighed the competing evidence on the facts.

The Board, PSEG Nuclear and Exelon all cite the voluminous and detailed materials submitted by the applicants, apparently suggesting that the mere presence of these materials in the record is sufficient to sustain the Board's Orders. (BPUb28, PSb30-31, PSb32-40, EXb18-19) The Board and Exelon go so far as to suggest that N.J.S.A. 48:2-46 requires the Orders below to be upheld unless there is "no evidence" in the record to support them. (BPUb28, EXb26) To the contrary, the BPU is not exempt from settled standards of judicial review that require an

administrative agency to found its decisions on substantial evidence, and explain how that evidence supports the agency's determinations.

N.J.S.A. 48:2-46 provides, in its entirety, as follows:

> The Superior Court, appellate division is hereby given jurisdiction to review any order of the board and to set aside such order in whole or in part when it clearly appears that there was no evidence before the board to support the same reasonably or that the same was without the jurisdiction of the board.
>
> No order shall be set aside in whole or in part for any irregularity or informality in the proceedings of the board unless the irregularity or informality tends to defeat or impair the substantial right or interest of the appellant.

Far from suggesting a more lenient standard of review for the Board, this provision affirms that the Board, like other State agencies, is subject to judicial review, that there must be evidence in the record that "reasonably" supports the Board's decisions, and that Board Orders can be reversed for defects that "defeat or impair the substantial right or interest of the appellant." The clear intent of this language is that Board Orders, like those of other State agencies, must be "reasonably" founded upon the evidence in the record, and must give due consideration to disputed issues of fact.

Our courts have affirmed that the Board is subject to the fundamental obligation of an administrative agency to explain itself. In its brief the Board cites three decisions in which

Board decisions have been upheld despite an absence of detail. (BPUb36-37) Those same decisions make it clear that the Board's reasoning must be discernable. In In re PSE&G's Rate Unbundling, 167 N.J. 377, 392, cert. denied 523 U.S. 813 (2001), Board's decision to adopt a mid-range estimate of the value of PSE&G's electric generation instead of higher or lower estimates was upheld because it could be explained as an exercise of "[c]ommon sense ...." In N.J. Bell Tel. Co. v. Dep't of Pub. Utils., the court upheld the Board's decision to adopt a lower rate of return than had been recommended by a hearing examiner based on the Board's explanation that it had done so because "the company's financial status had been stabilized since the previous rate increase and that the then improving economic climate pointed to further improvement in the future." 162 N.J. Super. 60, 75-76 (App. Div. 1978). N.J. Dept. of Public Advocate v. BPU upheld an Order in which the Board had rejected an administrative law judge's recommended rate increase because the Board's Order "not only make clear that the Board gave consideration to the recommendations of the ALJ, but in fact concurred with many of them." 189 N.J. Super. 491, 506-07 (App. Div. 1983).

These decisions make it clear that the Board, like other New Jersey state agencies, must explain the basis for its decisions in a manner that permits appellate review. It is not

sufficient that the record contains evidence that the Board could have relied upon to support its decision. The Board was obligated to explain why it credited that evidence as to the key issues in dispute. While there is no question that applicants provided "reams of financial data" (PSb32), determinations of fact do not necessarily follow from the quantity of evidence offered, but rather the "quality, accuracy and credibility of the testimony adduced, the reasonable inferences deducible, and the entire circumstances surrounding the case." Fornarotto v. Bd. of Pub. Util. Comm'rs, 105 N.J.L. 28, 32-33(N.J. Sup. Ct. 1928)(citations omitted) The lengthy recitations in each of the three Orders below certainly reflected the Board's awareness of the materials in the record. However, it is not possible to discern from the Board's Orders how it resolved each of the key disputed issue of fact, including the fundamental issues of credibility that were raised below. The Orders below simply do not provide this Court with an explanation of "how [the Board] weighed the proofs," as is required for proper appellate review. St. Vincent's Hospital v. Finley, 154 N.J.Super. 24, 31 (App. Div. 1977).

The Court should reject the attempts by PSEG Nuclear and Exelon to supply the rationales that are missing from the Board's Order. These two Respondents devote many pages to arguments that their positions on various factual issues were

correct. (PSb45-49, EXb28-34). The rationales suggested by PSEG Nuclear and Exelon were not articulated in the Board's Orders, and therefore do not satisfy the Board's obligation to explain how it weighed the evidence. As our Supreme Court has recognized, "'[t]he grounds upon which an administrative order must be judged are those upon which the record discloses that the action was based[,]'" and not upon an after-the-fact explanation of the administrative agency's decision. In re Petition of Elizabethtown Water Co., 107 N.J. 440, 460 (1987),quoting Securities and Exch. Comm'n v, Chenery Corp., 381 U.S. 80, 87 (1943).

The Court should also reject the Board's suggestion that the lack of analysis in its Order should be excused because the record includes information that is claimed to be confidential. (BPUb32) The Board cannot seriously contend that it could not have explained the reasons for its key factual determinations without reference to confidential information. Further, to the extent confidential information was necessary for a fuller explanation the Board could have issued its Order in "public" and "confidential" versions, thus making the Board's reasoning available at least to those parties entitled to receive the protected information, and to this Court.

The Board, PSEG Nuclear and Exelon all argue that the ZEC Act required the Board to accept some elements of the "cost"

side of the applicants' financial projections. These arguments focus on N.J.S.A. 48:3-87.5(a) which provides, in part, that the ZEC applications are to include:

> certified cost projections over the next three energy years, including operation and maintenance expenses, fuel expenses, including spent fuel expenses, non-fuel capital expenses, fully allocated overhead costs, the cost of operational risks and market risks that would be avoided by ceasing operations, ...

According to the Respondents, this provision means that (1) the statute prohibits the Board from considering the fact that the risks of negative financial results may be mitigated by the potential that costs may be lower or revenues may be higher, (2) that costs must include a spent fuel charge that has been suspended and that may never be paid by the units' owners, (3) that the costs must include "flow through" recovery of capital expenditures, and (4) that the applicant's quantification of "fully allocated overhead costs" must be accepted even if they include costs that would not "be avoided by ceasing operations." (BPUb28-30, PSb45-46 PSb48-49 & n. 31, EXb30-33)

While Board's rejection of Rate Counsel's and the IMM's positions on these issues in the first ZEC proceeding was affirmed in the ZEC I Affirmance, the legal context of the second ZEC proceeding is different. In the proceedings below, the Board had the authority and the responsibility to determine what level of subsidies was actually needed. Thus, the Board

should have considered the reliability and accuracy of the applicants' methodologies for quantifying costs. Given the applicants' own acknowledgement that they did not need the full amount of the subsidies indicated by their financial projections, there was clearly a substantial dispute as to the reliability of those projections, which the Board was obligated to address. The ZEC I Affirmance does not foreclose such an analysis.

With regard to the costs of risks, the Board and PSEG Nuclear argue that the Board was bound to reject Rate Counsel and the IMM's evidence that the applicants overstated their costs of risk because they failed to consider the likelihood that their revenues could be higher, or their costs, lower, than anticipated. (BPUb29, PSb45-46) There is, however, no clear prohibition on the consideration of "upside" risks in the language of the ZEC Act. The statute provides that:

> "operational risks" shall include, but need not be limited to, the risk that operating costs will be higher than anticipated because of new regulatory mandates or equipment failures and the risk that per megawatt-hour costs will be higher than anticipated because of a lower than expected capacity factor, and "market risks" shall include, but need not be limited to, the risk of a forced outage and the associated costs arising from contractual obligations, and the risk that output from the nuclear power plant may not be able to be sold at projected levels.
>
> N.J.S.A. 48:3-87.5(b) (emphasis added)

This language provides that the Board's consideration of risks "need not be limited to" the elements specified in the statue, and thus allows the Board discretion to consider other components of risk. Rate Counsel and the IMM suggested nothing more than the common-sense proposition that the potential for events that positively affect earnings will reduce the overall risk of a negative event. The language of the ZEC Act does not prohibit the Board from considering the applicants' failure to consider "upside" risks in determining whether they had demonstrated the need for subsidies.

The ZEC I Affirmance did not specifically hold that "upside" risks may not be considered. The Court held that operational and market risks may not be excluded from the Board's analysis. 467 N.J. Super. at 181. However, the Court did not directly address the issue of whether the applicants' overall costs of risk were overstated because of the failure to consider the potential for profits in excess of the applicants' projections. In this regard, it is important to note that neither the IMM nor Rate Counsel ever proposed "[z]eroing out" the costs of risk, as the Board asserts at page 29 of its brief. As the Board acknowledged in the three Orders below, both Rate Counsel and the IMM maintained that risks had been improperly quantified by the applicants. (Aa424-25, Aa426, Aa491-92, Aa493; Aa558, Aa559-60) This is not "zeroing out" or disregarding

risk, it is calling the Board's attention to a fundamental flaw in the applicants' analysis.

The ZEC Act also does not unambiguously prohibit consideration of Rate Counsel's and the IMM's evidence on other elements of the applicants' cost projections. While the ZEC Act includes "spent fuel expenses" as a cost element, it does not specify whether the legislature's intent was to compensate for costs that are not actually being paid, and may never be paid, by the nuclear units' owners. N.J.S.A. 48:3-87.5(a). Similarly, while "capital expenses," are a cost element, the statute does not specify that unit owners must be compensated for capital investments on a "flow through" basis. Id. Finally, the statute does not permit recovery of "fully allocated overhead costs" even if they are not avoidable by shutting down the nuclear unit. The ZEC Act explicitly provides that all cost elements, including this one, must be considered only if they "would be avoided by ceasing operations ...." Id. Thus, the Board was permitted to consider Rate Counsel's evidence that some of the units' projected costs for support services and overhead were not avoidable. Rate Counsel did not seek to exclude risks, but rather sought proper quantification of those risks.

The ZEC I Affirmance likewise did not prohibit consideration of these issues. The Court held, as provided in

the ZEC Act, that the cost elements specified in the statutes must be considered. 467 N.J. Super. at 181. However, the Court did not hold that the applicants' quantifications of these costs may not be challenged. Rate Counsel's evidence on these issues should have been given due consideration by the Board, but the Board's Orders do not reflect that this was done.

In addition to the evidence on costs, the Board was also obligated to consider disputed factual issues relating to revenues. None of the Respondents assert that the Board was prohibited from considering Rate Counsel's or the IMM's evidence regarding the applicants' projected revenues for the nuclear units. Rate Counsel's and the IMM's evidence on the proper quantification of projected energy and capacity revenues for the three nuclear units should have been considered by the Board. In addition, the Board should have considered Rate Counsel's evidence that revenues were understated because they did not include hedging revenues or tax benefits. The Board's Orders indicate it was aware that these issues had been raised. (Aa427-28, Aa494-95, Aa561-62). However, the Orders contain no analysis demonstrating that these issues were given due consideration by the Board.

The three Orders below make it clear that the Board's determination to award ZECs, and its determination not to reduce the amount of the subsidy, were not based on a reasoned and

careful analysis of the evidence in the record. They confirm, as detailed in Rate Counsel's initial brief (Ab2, Ab15-16), that the determinations below hinged not on the record as a whole but on a single fact — the applicants' threat to close the nuclear units if they did not receive the full $10 per megawatt-hour subsidy. The basis for the Board's decision was described most succinctly by Commissioner Robert Gordon, who observed that all of the analysis performed by the Board's consultant and others was apparently "a meaningless exercise," and acknowledged that the result of the proceeding below was dictated by the applicants' "intransigence" in demanding the full $10 per megawatt hour. (Aa389)

Contrary to Exelon's argument (EXb38-39), the issue is not the credibility of the witness who testified to the applicants' demand for the maximum subsidy. The issue is whether it was proper administrative decisionmaking to accept a number that was based, not on any objective financial analysis, but rather on the fact that, as publicly stated by Ralph Izzo, President and CEO of PSEG Nuclear's parent corporation Public Service Enterprise Group, $10 per megawatt hour is "all the state can do." (Aa361, Aa368-69, see T107-2 to T107-16) While it is understandable that the Board would be concerned that the applicants would follow through on their threats to shut down

the nuclear units, this is not the objective financial analysis contemplated in the ZEC Act.

In an apparent attempt to minimize the importance of careful review by the Board, PSEG Nuclear and Exelon have cited provisions in the ZEC Act which they contend will protect ratepayers from paying excessive subsidies. (PSb12, EXb12-13) It is important to recognize that these protections are limited.

As noted by PSEG Nuclear an Exelon, the ZEC Act provides for reductions of the subsidies granted to a nuclear plant if the plant receives revenues from other sources for its "fuel diversity, resilience, air quality, or other environmental attributes ...." N.J.S.A. 48:3-87.5(e)(4) & (i)(3) (PSb12, EXb12) However, there are no refunds if the units receive subsidies for other reasons, if costs are lower than projected, or if revenues increase due to changes in the energy and capacity markets. Id. Also, such refunds are not immediate or automatic when the unit begins to receives the other subsidies. The Board must first make a determination that such revenues have been received, and only then may reduce the number of ZECs the nuclear unit receives "on a prospective basis ...." N.J.S.A. 48:3-87.5(i)(3). Further, as Rate Counsel explained in one of its briefs to the Board (PSca364), actually applying this provision may present some challenges. For example, if, instead of receiving direct subsidies the nuclear units benefit

indirectly from a carbon tax or other regulatory change intended to compensate for the units' attributes, the applicability of the provision may be disputed, and benefits may be difficult to value.

This provision is scant protection against subsidies that turn out to have been too high. There is no mechanism to determine whether subsidies were actually needed to keep the units open, or to recapture excess profits that occur for any other than the limited reasons provided in the statute.

PSEG Nuclear and Exelon also cite N.J.S.A. 48:3-87.5(k)(2), which provide for refunds of ZEC revenues if a unit retires during a ZEC eligibility period. (PSb12, EXb13) However, refunds are not required if the unit closes for any of several enumerated reasons including the enactment of a new State tax on electric generation, the enactment of a State or federal law that materially reduces the value of a ZEC, or the need for unanticipated capital expenditures in excess of $40 million. N.J.S.A. 48:3-87.5(k)(1) & (k)(2). It is entirely possible that the units could close after collecting many years of ratepayer-funded subsidies, with no recourse for ratepayers.

In reality, the consumer protections cited by PSEG Nuclear and Exelon are limited, and ratepayers must rely on the Board to perform a thorough review to ensure that subsidies from ratepayers to unregulated generators are in fact needed. This

review, not the limited provisions cited by the Respondents, is the one true protection afforded ratepayers under the ZEC Act. That protection was not provided in the three Orders below.

CONCLUSION

In the proceedings below, the Board failed meet its fundamental obligation to justify its decision based on the evidence in the record. The three Orders below are arbitrary and capricious and should be reversed.

Respectfully submitted,

STATE OF NEW JERSEY
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Dated: March 14, 2022