Closing the Accountability Gap...

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This is an opportunity that an investor-owned utility like New Jersey American Water seeks out as a good way to achieve customer and rate base growth since very little of New Jersey is available for further development.

Unfortunately, there is a misperception about private ownership of water systems. When New Jersey communities have sought to offer their systems for sale, typically by referenda, some environmental organizations and a national organization with a strong New Jersey presence, Food and Water Watch, campaigned heavily to organize opposition to the resolution, and if it passes, to the sale. They believe that since water is necessary for life, it should not be owned by corporations; however, this argument fails to recognize that locating, accessing, treating and delivering water that meets safe drinking water standards cannot be done for free. The argument also fails to acknowledge that increasingly, some municipalities struggle to meet their drinking water quality obligations because of how resource-intensive it is. It would be nice if safe drinking water were free, but the reality is, people willingly pay considerably more for bottled water because they believe it is safe, even when it is no safer than what is delivered from the tap by highly regulated investor-owned water utilities.

New Jersey's Water Quality Accountability Act, if enforced equally irrespective of water system ownership, is an important step towards ensuring safe drinking water statewide in any community with a public water system.

QUESTIONS? CONTACT US AT: 856.840.4187 OR MEMBERSHIP@NJUSA.US
FOR MORE INFORMATION ON NJUSA, VISIT: WWW.NJUSA.US

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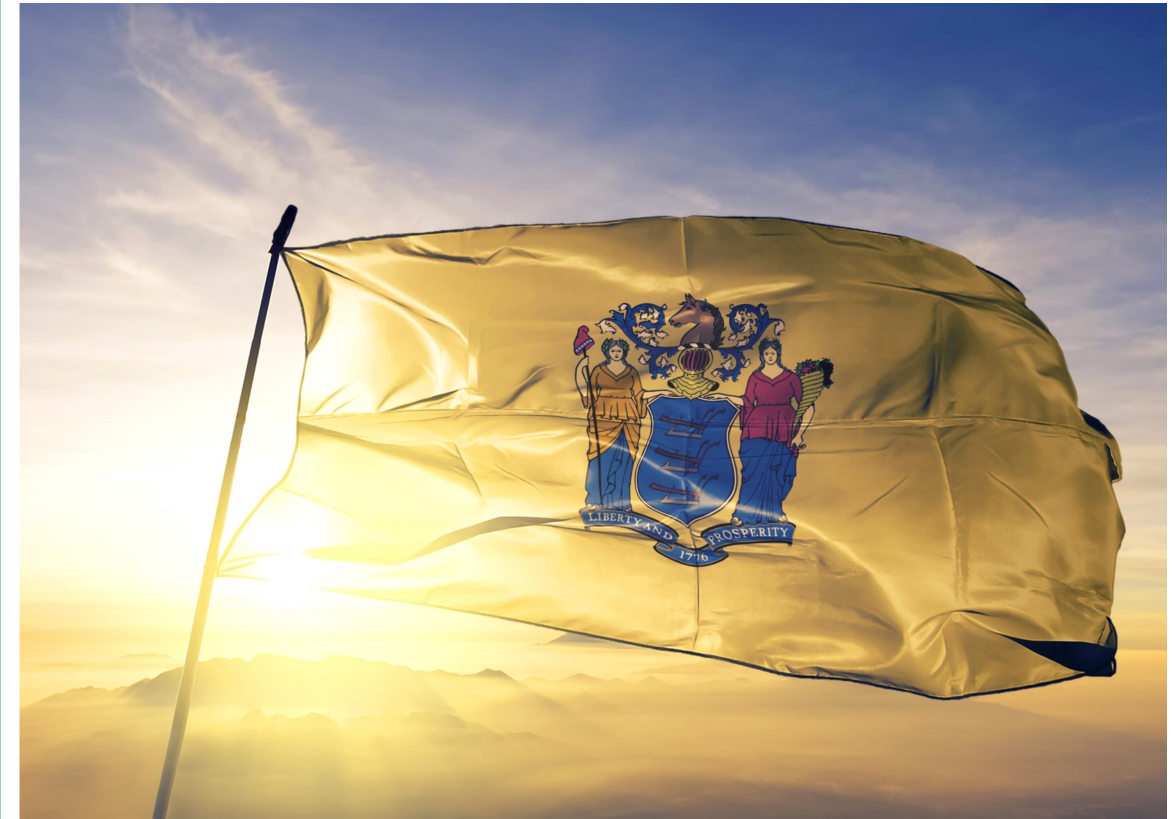
We wish all of our members well during these uncertain times. COVID-19 has diminished everyone's ability to gather in groups, including NJUSA. The event listed in this newsletter is tentative, pending decisions by the State and what we think is best for our staff and members. We will continue to monitor the situation and advise members accordingly.

Volume 6, Issue 1



NJUSA Insight

NJUSA Comments on BPU's Energy Efficiency Proposals

New Jersey's Energy Master Plan (EMP) was released in January. While it is the most prominent energy policy development of 2020, it is not the most imminent or consequential in the short-term for utility shareholders. The most significant pending state energy policy development is the Board of Public Utilities (BPU) staff's proposal to achieve the energy efficiency mandate of the Clean Energy Act of 2018 (CEA). The CEA requires natural gas utilities to reduce average annual consumption by 0.75 percent and electric utilities to reduce average annual consumption by 2 percent over the past three years within five years of starting their programs.

NJUSA filed comments on individual aspects of the proposal issued earlier in the year and on the final staff proposal issued in March. The issues of greatest potential impact on the value of utility shares include: who will administer energy efficiency programs—utilities, BPU contractors or both; what performance targets the utilities will have to meet; what the incentive and penalty structures required under the law should be; what the basis should be for establishing the level of return allowed on energy efficiency investments; the timing of cost recovery of energy efficiency investments; and how to make utilities whole when revenues are lost as a result of the mandate to help customers use less electricity and natural gas.

While BPU made some modifications to its final proposal, significant concerns remain. NJUSA therefore submitted comments on the final staff proposal focusing sharply on the economic realities that affect shareholders' investment decisions. The key points of our comments are summarized below.

NJUSA appreciates BPU staff's work to advance energy efficiency goals under a very aggressive schedule and that some of the concerns we raised previously were considered. Still missing though is an understanding of why people like NJUSA's members choose to put their limited investment dollars in New Jersey utilities—they expect and need to earn a fair return on their investment and to do so, the utilities must be

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A MESSAGE FROM THE PRESIDENT

Dear Members,

We hope this finds you and your families healthy and managing as well as possible in these challenging times. June is near, a time when normally we would be gathering for the Annual Luncheon and considerably further along in the year than normal for our first newsletter. In all respects, COVID-19 has caused 2020 to be unlike any year in the memories of most Americans. All of us at NJUSA are well, working remotely from our homes, continuing to focus on policy developments that can affect the value of your utility shares.

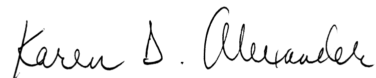
We have chosen the State Flag for the newsletter banner art in recognition of the extraordinary challenges and efforts being made by New Jerseyans to overcome and manage life in the midst of the pandemic. While we will have fewer newsletters this year due to budget constraints, we will endeavor to keep you abreast of significant policy developments that can affect the value of New Jersey utility investments.

The most prominent policy development thus far is the work of the State to advance its climate change-focused energy agenda, with the issuance of the final Energy Master Plan (EMP) in January and a major energy efficiency proposal in March. Fortunately, the EMP did not, as had been advocated by some environmental organizations, establish a moratorium on natural gas. That is a good outcome, as research thus far makes it clear that to do so could have significant negative effects, including potential insufficient gas supply in peak season winter months.

The other major energy policy development is BPU's implementation of the Clean Energy Act of 2018 which requires all New Jersey electric and gas utilities to conduct energy efficiency programs to make significant annual reductions in the use of electricity and natural gas by their customers. While the energy utilities have conducted energy efficiency programs in the past, and are willing and able to do so in the future, mandatory programs subject to performance standards and potential penalties raise significant concerns. We report on the BPU staff's energy efficiency proposal and NJUSA's advocacy on it in this issue of the newsletter.

The BPU is constrained like most organizations to observe social distancing and has been holding it's meetings virtually. NJUSA continues to monitor and participate in BPU activities remotely and will continue to press BPU to keep utility investors front-of-mind in all of its major policy decisions.

With warm regards and best wishes for you and those you hold dear,



Karen D. Alexander
President

*Schedule of Events**

Tentative

North Jersey Lunch & Learn
Wednesday, September 9,
12 p.m.
Holiday Inn
Hasbrouck Heights
12 to 2 p.m.
Registration begins at 11:30 a.m.

*** PLEASE NOTE**
We are actively monitoring circumstances related to public gatherings and COVID-19. Events we hoped to have in June and July have had to be cancelled. As always, our first priority is to the health and wellbeing of our staff and members. It is not yet clear whether the September luncheon in Hasbrouck Heights will be allowed or advisable, so we ask for your patience as we attempt to ensure we hold events that will not only be informative but safe for all. We will let you know as early as possible if the September event will be held. Please stay well!

NJUSA's Energy Efficiency Comments

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financially strong. It is not only utility investors that rely on strong utilities, the health and wellbeing of all New Jersey's residents and businesses depend on the ability of New Jersey utilities to attract and retain investment capital. Accordingly, NJUSA's comments focus on areas of staff's final proposal that, absent modification, will discourage investment and diminish utilities' ability to meet both traditional infrastructure needs and the State's new energy efficiency goals.

The ROE. The ROE deduction for energy efficiency investments makes a dollar spent on energy efficiency less valuable than a dollar spent on pipes and wires. The deduction is contrary to the belief staff expressed on page 10 of the Straw Proposal: "…that, while required by statute, energy efficiency programs will not ultimately be successful if the proposed mechanism negatively impacts a utility's economic bottom-line …or if such programs are considered a less attractive investment than traditional infrastructure." This is a disconnect that must be remedied if the programs are to succeed.

Also, the proposed ROE construct rests on a faulty premise, "to reflect the reduced risk associated with guaranteed, contemporaneous recovery of program investments." That trade-off is apt in the context of traditional infrastructure investments where most of what affects the utility's performance is within its control. Utility shareholders are familiar with utilities' management of operational and regulatory risk attendant to infrastructure investments. But, there is no similar base of experience for shareholders to anticipate utility performance under mandatory energy efficiency programs. Considering the order of magnitude increase in participation needed to meet the energy efficiency goals, and the prospect of a deduction to the ROE even if performance targets are met, shareholders would likely view investment in New Jersey's electric and gas utilities to have become considerably more risky and less attractive than before. Under the current proposal, there is no clear or compelling reward for shareholders to fund these programs, and thus no reason to expect they would choose to do so.

The penalties and incentive structure. For shareholders, performance targets with penalties that are not informed by New Jersey-specific experiences exacerbates the perception of risk associated with investment in New Jersey utilities performing mandatory energy efficiency programs. A penalty structure informed by a base of real-world experiences can enable the utilities not only to demonstrate what is achievable in their service territories, but also for the Board and the utilities to see the real world implications on capital availability. It can also avoid judging utility performance during the transition period against standards not reflective of actual New Jersey experience when there will undoubtedly be unforeseen challenges. The Board should use the first Triennial period to establish a performance baseline for each utility's service territory.

The 7-year amortization period. Seven years seems arbitrary. A longer amortization could be beneficial both to shareholders, who could earn a return over a longer time, and to customers, whose bill impacts would be minimized. This is yet another way to encourage—or, if set too short—discourage, investment.

The lost revenue mechanism. The proposal puts in place a limited revenue adjustment mechanism (LRAM) that recovers the impact of utility-run efficiency programs only. It also allows the Conservation Incentive Program (CIP) mechanism to continue and encourages electric utilities to adopt a CIP. However, the LRAM puts utilities at risk of not recovering the impacts of the programs that are run by others and thus not within their control. Further, the LRAM does not recognize the fact that the circumstances present when the existing CIPs were instituted are not comparable to the circumstances that exist today—there were no aggressive goals and performance mandates. The difference is even more stark in light of the proposed penalties and ROE reduction.

The lost revenue mechanism should be based on current-day realities; address shareholders' expectation that utilities be able to earn their allowed return; ensure utilities are made whole for the revenues lost from helping customers use less energy as the state requires; and not expect shareholder equity to be a source of funding.

Finally, without the advent of COVID-19, the ability of utilities to meet the aggressive energy efficiency goals was in question. The pandemic poses questions no one can yet answer. For example, when will social distancing end and the economy recover? When will the utilities' energy contractors be fully staffed and ready to start the work? When will utility customers be ready to accept utilities' offers to save energy and money enough to let contractors into their homes to conduct energy audits? Will businesses that survive the pandemic have energy efficiency as a priority?

We urge the Board to fully address the issues we've raised and be especially cautious in these uncertain times to ensure that in advancing energy efficiency, utility shareholders not be discouraged to continue their investments.