

Public Service
Electric and Gas
Company

E. James Ferland
Chairman of the Board
and Chief Executive Officer

80 Park Plaza, Newark, NJ 07101 201-430-5620 Mailing Address: P.O. Box 570, Newark, NJ 07101

May 19, 1997

The Honorable John D. Dingell, Ranking Member
Commerce Committee Democratic Office
U.S. House of Representatives
564 Ford House Office Building
Washington, D.C. 20515

Dear Congressman Dingell,

I appreciate the opportunity to participate in your fact-finding on the vital issue of electric industry restructuring. My responses to your questions are attached. Please don't hesitate to call on me directly or contact our Washington representatives (Patsy Thompson, Roger Schwarz; 202 408-0800) should you have further questions as this important public policy debate continues.

Sincerely,

A handwritten signature in black ink, appearing to read "E. James Ferland". The signature is stylized with a large, sweeping "E" and a long, horizontal stroke extending to the right.

1. **From your company's point of view, is it necessary for Congress to enact legislation bearing on retail competition, and why? If you favor legislation, please outline which issues should be addressed and how you think they should be.**

As individual states move toward adopting retail competition plans, PSE&G would support comprehensive federal legislation that addresses the following key areas:

- Providing a fair and reasonable opportunity for full recovery of transition costs.
- Providing uniform, equitable environmental standards for all electricity producers;
- Providing reciprocal treatment for access to retail markets across state and jurisdictional boundaries;
- Defining clearly and resolving state/federal regulatory responsibilities;
- Establishing rules that put investor-owned and public utilities on an equal footing;

2. **If the state(s) you serve has adopted or is considering adopting retail competition, what are your biggest concerns?**

The N.J. Board of Public Utilities, on April 30, issued an Energy Master Plan for our state that will provide retail choice to all customers by the year 2000. PSE&G supports the move to competition and also supports the aggressive timetable included in this plan. We believe the critical concerns in making this transition are to ensure that all customers benefit from competition, reliability and availability of electric service are not compromised, and investors are treated fairly through full recovery of transition costs.

A key point in this regard is that not one dollar of utility investment becomes stranded unless and until government changes the rules under which these investments were made. The N.J. plan provides utilities with "an opportunity" to recover transition costs, which, in turn, allows for the possibility of insufficient recovery and unfair treatment of investors.

3. **Whether or not you favor federal legislation, please indicate your position on the following specific issues:**

(a). A federal mandate requiring states to adopt retail competition by a date certain. If retail competition is under consideration in the state(s) you serve, do you believe Congress should provide additional direction or authority?

As more and more states take up the retail choice issue, a federally mandated date certain for retail competition would help meet requirements for market reciprocity, and, once established, strike from the list one potential state-federal jurisdictional issue.

(b). Recovery of stranded investment. If the state(s) you serve already has adopted retail competition, how was this issue addressed and are you satisfied with the outcome? If your state(s) is considering adopting retail competition, how would you recommend that this issue be treated? Do you think Congress should enact legislation relating to stranded cost issues, and if so, what would you recommend? Is securitization a useful mechanism for dealing with stranded costs and whom does it benefit?

As noted, the N.J. Board of Public Utilities has issued a retail competition plan that would provide utilities the opportunity to recover up to 100% of stranded costs. The plan, however, does not guarantee recovery of any portion of these costs and indicates that stranded cost recovery should not be allowed to negatively impact achieving the goal of a 5%-10% rate minimum rate reduction for all customers.

PSE&G believes that fair treatment for the investors who have provided the capital necessary for building the world's best electric power infrastructure requires 100% recovery of stranded costs. What is sometimes ignored in this debate is the fact that regulators contributed to the creation of stranded costs by extending depreciation schedules for utility plant and facilities in an effort to keep rates as low as possible. Also, regulators nationwide have exercised their authority to disallow recovery of utility investment deemed imprudent, unnecessary, or mismanaged. Investment now on the books has passed these tests and shareholders deserve recovery of these costs.

Stranded cost recovery is a critical for fair treatment for millions of utility shareholders nationwide, many of whom depend on proceeds from this investment for their livelihoods, and is also essential for establishing a vigorous and robust competitive market. We believe, therefore, that Congress should include a mandate for stranded cost recovery in electric restructuring legislation.

Securitization is an extremely useful mechanism for stranded cost recovery. When properly structured, securitization will provide benefits to both ratepayers and utilities by making immediate rate relief both possible and financially sound.

(4). If Congress enacts comprehensive restructuring legislation, should it mandate "unbundling" of local distribution company services? What impact would this have, and would the effects differ for various customer classes? Would this entail substantial expense, and who would incur any such costs?

Nearly every state - including New Jersey - that has either adopted or is considering

adopting retail competition, has called for the unbundling of electric costs and services. We believe that unbundling is necessary for establishing competitive markets for these services and that this can be accomplished without undue expense or burden on service providers or customers.

- (5). Recently Chair Moler of the Federal Energy Regulatory Commission recommended that, as part of comprehensive legislation, Congress authorize the commission to enforce compliance with North American Electric Reliability Council standards to help maintain reliability of service. Do you believe this is necessary and why or why not?**

Currently, all electric generators in the mid-Atlantic region served by the Pennsylvania-New Jersey-Maryland (PJM) power pool have committed to comply with NERC reliability standards and we would support the requirement for all market participants, including utilities, power marketers, independent power producers, and regional Independent System Operators (ISO) to abide by these standards.

- (6.) What concerns does your company have with respect to the role of public power and federal power marketing agencies in an increasingly competitive wholesale electric market? In markets in which retail competition has been adopted? Are there concerns you would like to have addressed if Congress enacts comprehensive restructuring legislation? Should Congress consider changes to federal law as it applies to regulation of public or federal power's transmission obligations?**

Federal restructuring legislation must include components that provide for competitive parity between public power entities and privately-owned market participants. This means that all electric generators should be subject to comparable requirements and conditions, such as access rates and charges, reciprocity rules, reliability requirements, purchase mandates, antitrust penalties, and review of affiliate transactions.

Competitive parity also means equal treatment by federal, state, and local governments in matters of property, franchise, taxation, depreciation rules, and financing costs. Today, for example, public power facilities typically borrow funds at rates well below those available in private debt markets. This is a built-in cost advantage that should not be allowed to continue in a competitive market. It is especially vexing when public power entities and federally subsidized power marketing administrations use financial advantages and tax-supported subsidies in local and regional competition for jobs and economic development. It's important that federal legislation requires that public power entities that seek to do business outside of their jurisdictional fences play by the same rules as all other market participants.

- (7). If Congress enacts comprehensive restructuring legislation, should changes be made to federal, state, or local tax codes, and if so, why?**

Tax inequities between utilities and nonutility power suppliers have been a factor in wholesale competition in New Jersey and elsewhere around the nation. Independent power producers and cogenerators, to a large extent, are not subject to the franchise, revenue, and other taxes that states and local governments have levied on utilities. While we should be cognizant of the role utility taxes have played traditionally in supplying state and local governments with revenue that support important services, we also need to make the transition to a tax system that treats all market participants fairly and uniformly. It would be appropriate for federal legislation to direct states to examine energy tax treatment within their jurisdictions and correct inequities that exist.

Federal legislation can also enhance the ability of states to address the stranded cost issue by minimizing tax implications of securitized bonds.

- (8). What, if any, concerns do you have about the reliability of the electric system? If the industry moved to retail competition, will adequate reserves be available? Is the transmission system capable of handling full retail competition?**

Retail competition and system reliability with concomitant adequate capacity reserves are entirely compatible. As noted in the response to question 5, it's our belief that regional Independent System Operators will assume the role previously played by regional power pools in monitoring and maintaining system reliability.

PSE&G is concerned, however, that if the current system of unequal environmental standards is carried over into a restructured industry, capacity reserves will be maintained by continued operation of old, dirty generating facilities and investment in new, clean generation will be delayed and displaced. This has serious economic and public health implications for New Jersey and the Northeast which bear the burden of air emissions produced in other regions of the country and carried into our region by prevailing winds.

In regard to the ability of the transmission system to handle full competition, the critical issue involves adequate pricing. If transmission services are priced correctly, investment in facilities will be encouraged and the grid won't become overly congested. If, however, these services are underpriced, the potential exists for transmission congestion, delays, and system strain.

- (9). If Congress enacts legislation on retail competition, should changes to the Public Utility Holding Company Act (PUHCA) be included? If so, what would you recommend? In particular, how should Congress address market power concerns in any such legislation? Are transition rules needed during the period before effective competition becomes a reality?**

PSE&G does not believe that federal restructuring legislation needs substantial

provisions to address the market power concern.

FERC has adequate authority and adequate ability to investigate and act in regard to market power. In addition, the various federal antitrust and fair trade statutes are available to the Justice Department as further safeguards.