January 11, 2016

Mr. Stuart Spencer  
Chief, Air Division  
Arkansas Department of Environmental Quality  
5301 Northshore Drive  
North Little Rock, AR  72118-5317


Dear Mr. Spencer:

I am writing on behalf of the Municipal Energy Agency of Mississippi (“MEAM”), a co-owner of the Plum Point Energy Station in Osceola, Arkansas. My purpose in writing is to follow up on a topic I raised during the ADEQ’s Section 111(d) workgroup conference of November 18, 2015 – namely, the uniquely adverse effects that the early retirement of a generating unit would have on municipal owners, who typically finance their ownership in generating units through the issuance of long-term revenue bonds. This topic was broadly alluded to during the January 5, 2016 stakeholder meeting as “Stranded Investments” (see slide 4 of Tricia Jackson’s presentation on “Key Takeaways” from the stakeholder conferences), but, from Tricia’s later presentation on “Key Issues and Concepts” being considered for inclusion in the ADEQ’s January 21, 2016 comments, doesn’t appear to be one that ADEQ will address in its submission to EPA. I would encourage the ADEQ to consider addressing the matter in its upcoming comments, though, for two reasons: (1) the direct applicability of the issue to several of Arkansas’ most significant coal-fired generating stations; and (2) the fact that EPA has specifically invited comments that address the impacts of the proposed federal plan on small entities (see 80 Fed.Reg. at p. 65056). A suggestion on how MEAM’s concern might be addressed in ADEQ’s comments is offered below.

The unique impact of an early retirement on municipal utilities arises from the fact that municipalities and municipal joint action agencies finance their ownership of generating facilities exclusively through the issuance of long-term bonds. Typically, those bonds are secured by a pledge of revenues received from the sale of power to customers. In the case of a municipal joint action agency such as MEAM, the bonds are secured by the revenues the agency receives from its members (participating municipal electric systems) pursuant to a set of power sales contracts specific to each generating project in which the agency acquires an interest. In MEAM’s case,
those contracts obligate its members to make payments to MEAM with respect to the costs of Plum Point, including payments of principal and interest on the bonds issued to finance MEAM’s 6.0% share of that station, on an unconditional “take-or-pay” basis. What this “take-or-pay” commitment means is that MEAM must set rates to its members at a level sufficient to pay debt service on the Plum Point project bonds, and the members must pay those charges, regardless of whether Plum Point is operating or operable. As a result, MEAM’s obligation to pay debt service on the bonds issued to finance its share of Plum Point would continue without reduction if the unit were retired early, or if its output were significantly reduced, in order for Arkansas to achieve compliance with the Clean Power Plan. Beginning in 2017, MEAM’s annual debt service obligation for its Plum Point bonds is approximately $5.8 million each year through 2040 (jumping to roughly $8.0 million in 2041), and MEAM’s members likewise are required to pay those amounts without regard to whether Plum Point continues to operate or is retired early as part of the state’s CPP compliance plan.

This scenario should be compared to the very different circumstances of an investor-owned utility (IOU). There are two important differences. First, IOUs do not use project-specific financing; rather, they finance new generating units from the company-wide pool of capital resources. While the IOU may issue new equity (stock) or debt to help pay for a costly construction project, that financing generally is not tied to any particular project. Second, unlike municipal utilities, IOUs are not 100% debt financed; rather, their capital resources include a substantial component of common equity (usually in the range of 30-50% of total capital). If an IOU is forced to retire a generating unit before it has recovered its investment in the unit through rates, it usually will be required to split the unrecovered costs between the company’s ratepayers and its shareholders. (FERC’s practice, for example, is to split any such loss more or less evenly between ratepayers and shareholders.) The portion the IOU is prevented from including in its rates will become a one-time charge against earnings, with a commensurate reduction in the net equity component of the capital structure. The equity component thereby acts as something of a cushion, absorbing a portion of the retired unit’s unrecovered costs consistent with the principle that investors should not earn a return on property that is not “used and useful” in serving the public.

Due to this difference in financial facts and circumstances, municipal entities have no choice but to continue charging their customers for the capital costs of an electric generating unit that is retired before the bonds it issued to finance the EGU are paid off. (The alternative – suspending or reducing debt service payments on the bonds – is not viable, because the resulting default would trigger costly litigation and greatly increase the municipal entity’s costs of financing in the future.) The municipal utility’s customers thereby suffer a “double whammy” – they must continue to pay for the bonds issued to finance the retired EGU, and also would bear the costs of any new generating unit built to replace the retired unit. For MEAM’s members, the resulting double-charge would greatly burden ratepayers and impede development and recovery in communities that already face a number of severe economic challenges.

The most direct way to avoid the above-described situation, of course, is for Arkansas to formulate and implement a CPP compliance plan that allows Plum Point to continue operating as one of the most efficient, low-emissions, state-of-the-art coal-fired generating stations in the
country.\textsuperscript{1} If an EGU’s continued operation is adversely affected by a state’s compliance strategy, however, there should be flexibility in the proposed Federal plan to mitigate the resulting burden on the customers of municipal utilities that financed the EGU with long-term debt. For example, in its request for comments on the proposed Federal plan, EPA notes that the allocation of emission allowances to load-serving entities (LSEs) is a viable way of ameliorating adverse impacts on consumers:

Allocation to LSEs can help mitigate bill impacts on electricity consumers when applied in concert with certain additional design features. In particular, if LSEs commit and/or are required to pass through to ratepayers the value from their selling of the allocated allowances, this approach can mitigate the impact of electricity bill increases on consumers that might otherwise result from application of the federal plan.

80 Fed.Reg. at p. 65018. MEAM would favor an allocation of allowances to municipal utilities that face the potential “double-whammy” effect of CPP compliance described above. An allocation of allowances would serve to ameliorate the dual burden to consumers of paying rates that include both debt service on an early-retired EGU and the costs of a replacement source of supply. A stipulation that the LSE be obligated to pass through to ratepayers any proceeds it realizes from a sale of the allocated allowances, coupled perhaps with periodic reporting or audit requirements, would not be unreasonable in MEAM’s view.

We hope that the ADEQ will consider the foregoing and give thought to reflecting MEAM’s concerns and recommendation in its forthcoming comments on the proposed Federal plan. There are a number of EGUs in Arkansas in addition to Plum Point that are owned in whole or part by municipal utilities, and those utilities very likely would face the same dual-payment burden as MEAM if their EGUs were forced to retire early. By the same token, an allocation of allowances to such entities, coupled with a pass-through requirement, could have significant value in ameliorating the adverse rate impacts on consumers.

\textsuperscript{1} In fact, due to its very recent vintage (placed in service in 2010), Plum Point employs best available control technology to control emissions of nitrogen oxide (NOx), sulfur dioxide (SO\textsubscript{2}), mercury, and particulate matter. The plant was designed to comply with all emissions regulations and permit conditions, including previously-enacted mercury regulations. The air quality control systems include low NOx burners, overfire air and a selective catalytic reduction system to manage NOx emissions, fabric filters to manage particulate matter, a powder activated carbon system to remove mercury, and a dry flue gas desulfurization (scrubber) system utilizing hydrated lime solution to remove SO\textsubscript{2}. 
Thank you for considering MEAM’s comments. Please feel free to get in touch if you have any questions regarding the foregoing.

Very truly yours,

[/s/ GARY J. NEWELL]
Gary J. Newell
Attorney for the Municipal Energy Agency of Mississippi

cc: Tricia Jackson, ADEQ
Geoffrey Wilson
Executive Director
Municipal Energy Agency of Mississippi