PR RULE MISC (90-4) (55FR43231)

**STATE OF NEW HAMPSHIRE**

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December 20, 1990

Carlton Kammerer, Director
State Programs
Office of Governmental and
Public Affairs
U.S. Nuclear Regulatory Commission
Washington, D.C. 20555

Dear Mr. Kammerer:

This is a late filed response to the NRC invitation to state regulatory agencies to comment on the draft NRC policy statement pertaining to "Possible Safety Impacts of Economic Performance Incentives." This commission previously submitted the essence of its position on nuclear plant incentives to NRC consultant Robin Martin in correspondence dated October 1, 1990, a copy of which is enclosed. These data were primarily derived from New Hampshire Public Utilities Commission (NHPUC) docket No. DR 89-244, regarding the Public Service Company of New Hampshire (PSNH) rate plan to emerge from bankruptcy. Seabrook "synergies", or savings projected to result from Northern Utilities (NU) management of the facility, constituted a major component of that case. The commissioners, in approving the rate plan, noted that NU's ability to achieve the rates set forth in the rate plan, depends in large part on its ability to achieve the projected Seabrook O&M savings.

In docket No. DR 89-244 (NU/PSNH acquisition), the record indicates that NU had testified before the Bankruptcy Court that what usually comes out of rate cases in which a large nuclear unit has been placed in service is that the regulatory agency imposes a performance clause on the nuclear unit which provides that if the plant operates at less than a certain capacity factor; i.e., instead of working sixty percent of the time, it only works forty percent of the time, the utility has to pay all the costs of the replacement power.



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The motivation that regulators have for routinely establishing performance incentive mechanisms for nuclear plants is to insulate ratepayers from some of the replacement costs resulting from inferior performance, given that ratepayers are saddled with the high capital costs whether the plant runs or not. The purpose of a performance mechanism is not to substitute for prudence review but to complement it.

The absence of a performance incentive for Seabrook in the NU/PSNH Rate Agreement prompted the PUC to state its concern in its decision approving the acquisition of PSNH by NU:

> [W]e do not believe that a properly designed performance incentive would alter fundamental assignments of risk under the Rate Agreement. The achievement of the projected 5.5 percent rate track depends in large part on achievement of the Seabrook synergies and the establishment of performance incentives would be consistent with this goal.
>
> Nonetheless, we agree with staff that it is not necessary at this time to establish a performance incentive program for Seabrook as a condition to approval of the agreement. We may impose such a performance incentive program, however, if it appears in the future that the expected Seabrook synergies are not being achieved. <u>We would do so only on finding that performance incentives would be constructive in minimizing rate increases and improving efficiencies without compromising the Seabrook safety concerns</u>, (emphasis added).

The foregoing reservation expressed by the NHPUC regarding potential safety concerns is precisely the subject of the NRC draft policy statement which, <u>inter</u> <u>alia</u>, reflects the commission's concern that certain forms of economic performance incentive regulation have the potential for adversely affecting nuclear operation and public health and safety and specifically identifies those methods or approaches that are of particular concern (e.g., use of sharp thresholds, measurement of performance over very short time intervals, lack of "null zone", and inappropriate reliance on SALP scores).

<u>NEW HAMPSHIRE EXPERIENCE WITH PERFORMANCE INCENTIVES</u>

New Hampshire was one of the first regulatory jurisdictions in the country to implement a performance incentive program to improve the availability of fossil-fired generating stations and, consequently, has a substantial amount of experience with respect to their design and application.

The so-called "incentive feature" was instituted in New Hampshire in 1980 in order to forestall the abolition by the legislature of PSNH's fuel adjustment charge which automatically flowed-through the entire replacement cost of controversial and extended outages at PSNH's coal-fired Merrimack Station.

In essence, this incentive mechanism known as "ECRM"[1] is comprised of the following design features:

1. Reasonable, attainable targets established by NHPUC based upon four year rolling average actual availabilities for specific unites.

2. Ninety percent recovery of replacement costs if targets are not met. Ten percent retention of fuel savings resulting from performance exceeding targets.

This ECRM incentive mechanism may be responsible for contemporaneous improvements in PSNH fossil-fire generating plant performance.

NEW HAMPSHIRE PERFORMANCE INCENTIVE DESIGN FEATURES, IF IMPLEMENTED, WOULD MITIGATE THE NRC'S SAFETY CONCERNS

New Hampshire's current philosophy towards incentive design largely addresses the principle safety concerns expressed by the NRC. Specifically, the use of a four year rolling average for calculating availability targets resolves NRC's concerns with "measurement of performance over a very short time interval"; the recovery or refund of ninety percent of the change in energy costs which results from deviations from the PUC-approved availability targets addresses and resolves NRC's concern that a sharp threshold provides an incentive to continue plant operation to achieve a factor to avoid the large replacement power cost or achieve a substantial reward.

CONCLUSION

The potential reward or penalty under the existing incentive feature in New Hampshire is substantial enough to get management's attention but is not excessive so as to cause distortion to management's operation and maintenance policy and practices. Also, since targets are based upon data for four years, PSNH has been encouraged to optimize long-run availability rather than short run.

We recognize that caution is essential not to overstep the appropriate bounds of regulation and micro-manage the utility. Every company has a unique management style and philosophy, each

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[1] Energy Cost Recovery Mechanism

power plant is unique in its construction and operation. More importantly, the incentive program must be designed to enhance rather than diminish nuclear safety.

Incentive programs may be a benefit where traditional forms of regulation fall short in encouraging efficient management at reasonable cost. To the contrary, they could, if designed or implemented unwisely, serve as disincentives to nuclear safety.

The NHPUC's position is that an economic incentive program for Seabrook is not necessary at this time but if our ongoing review of Seabrook costs indicates a substantial failure to achieve projected savings the commission may revisit the issue. It is our opinion that an economic incentive program can be designed to achieve the dual objectives of optimum safety and reasonable costs.

Sincerely,

Larry M. Smukler

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Chairman

LMS/WEA/mag

DR 89-244

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October 1, 1990

Robin Martin
Battelle
P. O. Box C5395
4000 NE 41st Street
Seattle, Washington 98105

Dear Robin:

I enjoyed our discussion of September 28th regarding incentive regulation of nuclear power plants. As you requested, I have enclosed a copy of the transcript portions in which NU witness Opeka indicated that the NRC was not interested in incentive regulation of nuclear power plants. I have also enclosed a copy of our final order regarding the takeover of PSNH by Northeast Utilities as part of the plan for resolving the on-going PSNH bankruptcy.

In its order, the commission provided that NU shall meet with the NHPUC staff to determine what synergy related monitoring is appropriate. An incentive program could result from the monitoring effort if deemed necessary.

If you have any additional questions, please do not hesitate to contact me. I am looking forward to receiving your 1989 report on nuclear incentive programs.

Sincerely,

Wynn E. Arnold
Executive Director & Secretary