OHIO ENERGY GROUP

– Turning Energy Into Jobs –

House Bill 6
Proponent Party Testimony of Michael L. Kurtz
On Behalf of the Ohio Energy Group
Before the House Energy and Natural Resources Committee

May 15, 2019

Chairman Vitale, Vice Chairman Kick, Ranking Minority Member Denson and distinguished Members of the Committee, I am here today to give Proponent Party testimony regarding House Bill 6, known as the Ohio Clean Air Program.

My name is Michael L. Kurtz and I am General Counsel for the Ohio Energy Group. OEG is a trade organization formed in 2003 by large energy-intensive industrial companies with one or more plants in Ohio to promote low-cost, reliable electric power. Our 25 members spend more than $1 billion annually on gas and electricity and we provide more than 55,000 good paying direct jobs in Ohio.

I am testifying today as a proponent.

UPDATING THE EXISTING RPS AND ENERGY EFFICIENCY MANDATES IS SOUND POLICY.

Current law mandates that a specified amount of utility-sponsored energy efficiency savings be achieved (22% cumulative from 2009-2027), regardless of whether the programs are in the public interest. From 2014-2017 utility-sponsored energy efficiency program costs averaged $289 million per year. Sub. H.B. 6 eliminates these programs and authorizes the Public Utilities Commission to permissively authorize new energy efficiency programs only if they are cost-effective, in the public interest and consistent with state policy. This is a good change which protects consumers.

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Utility-sponsored energy efficiency programs require a group of ratepayers to partially pay for the more efficient appliances of their neighbors, and in some instances the production equipment of their business competitors. The person or business that gets the more efficient equipment enjoys a lower electric bill and understandably likes the program. But how do *you* benefit by chipping in for the costs of your neighbor's new central AC unit?

Utility-sponsored energy efficiency programs are decades old. The original justification came from the fully-regulated utility model. The argument was that increased conservation reduced the need for the utility's next power plant, which all ratepayers would have paid for. Now, this argument has almost no validity. We are no longer operating under a fully-regulated utility model. Currently, energy and capacity in Ohio is priced based on supply and demand considerations across the entire 13-state PJM region. Any benefit from delaying the need to build new generation is therefore not isolated to Ohio. Rather, the reduction in demand resulting from these programs provides benefits to all of PJM. In other words, utility-sponsored energy efficiency programs in Ohio benefit consumers in Pennsylvania and New Jersey just as much as here. When the energy efficiency mandates became part of Ohio law in 2008 the Ohio utilities still owned generation to serve native load and deferring the need to build new generation still had some economic validity. But that time has long gone. The Ohio electric utilities no longer build generation to serve native load and the rationale supporting stringent energy efficiency mandates no longer makes sense.

The other primary rationale used to justify utility-sponsored energy efficiency programs is environmental. Less energy used means less energy produced which means fewer emissions. No one disputes that conservation is good for the environment. But the question raised by Sub. H.B. 6 is whether utility-sponsored energy efficiency programs are a more effective means to help the environment versus directly paying Ohio-sited generators for each MWh of clean energy produced.

The purported energy savings from utility-sponsored energy efficiency programs should be viewed with caution. The first step in measuring the effectiveness of energy efficiency is an engineering estimate. This compares the energy usage of the old appliance versus the new one. This is easy. It is known as gross savings. But measuring net savings is very difficult for two well documented reasons. First, the "*free rider*" effect. Free riders are those businesses and individuals who would have done the same energy efficiency projects without funds from other ratepayers. If "*free*" money is available from other ratepayers why not take it? Second, the "*rebound*" effect. Utility-sponsored energy efficiency programs lower the bills of the recipients, which results in increased usage of the cheaper product. So long as the price elasticity of demand for electricity is not zero, the rebound effect holds true.

In contrast, Sub. H.B. 6 only pays for actual verified performance. Clean Air Resources get paid $9 only for each MWh actually produced in Ohio. Reduced Emission Resources get paid only if their CO2 emissions are cut.

Sub. H.B. 6 would make the renewable portfolio standard (RPS) voluntary, not mandatory. Currently, load serving entities in Ohio comply with the RPS mandates by buying Renewable Energy Credits (RECs), which represent one MWh of qualifying generation. Most RECs retired in Ohio were produced out-of-state. In 2017 (the most recent year where PUCO data is available), only 23.52% of the non-solar RECs retired in Ohio were produced in Ohio.

From 2014-2017, Ohio's electric distribution utilities and competitive retail electric service providers charged their customers $51 million on average per year for RECs. By 2026, the RPS compliance mandates will more than double. Redirecting these ever-increasing out-of-state REC dollars to incent clean generation in Ohio has the same regional environmental attributes as buying out-of-state RECs, but with attendant local economic development benefits like jobs and tax revenue.

It is important to recognize that the RECs produced in Ohio can be sold throughout the PJM region. This presents the opportunity for renewable developers in Ohio to receive a double benefit under Sub. H.B. 6: access to Ohio Clean Air Credits of $9/MWh plus revenue from selling RECs to out of state consumers. Despite this potential double benefit for Ohio sited renewable generation, I believe that the national renewable power developers largely oppose Sub. H.B. 6 because they are circling the wagons. They don't want a roll-back of Ohio's RPS mandates because it would hurt their narratives in other states where increasing RPS mandates are being forcefully pursued.

The price of RECs is largely a function of supply and demand across all of PJM. While Sub. H.B. 6 would reduce the demand for RECs in Ohio, other forces are moving in the opposite direction. In recent years, New Jersey increased its RPS to 50% by 2030, Maryland to 25% by 2020, Delaware to 25% by 2025, District of Columbia to 50% by 2032 and Pennsylvania 18% by 2020. All of these actions increased REC demand in PJM and therefore will increase the price of RECs produced in Ohio.

In 2015, West Virginia repealed its RPS mandate, Virginia's RPS goal is voluntary, and Kentucky has never had an RPS. Each PJM state has made very different RPS policy choices, which push and pull REC supply and demand in different directions throughout PJM.

To sum up, making the Ohio RPS voluntary would save consumers $51 million per year and elimination of the energy efficiency mandates would save consumers $287 million per year. This $340 million in combined savings is more than the $300 million price tag of Sub. H.B. 6.

SUBSTITUTE H.B. 6 WILL REDUCE ELECTRIC RATES FOR ALL CONSUMERS

Certain fossil fuel merchant generators argue that awarding Clean Air Credits to zero carbon generation will unreasonably "*distort*" the wholesale power market by supporting nuclear generation that might otherwise be forced to prematurely retire. "*Distortion*" is in the eye of the beholder. According to a March 19, 2019

Report by the Congressional Research Service[1], in 2017 the value of federal tax-related subsidies for the fossil fuel energy sector (primarily oil and gas) was $4.6 billion.[2] Also, "*distortion*" is an overused concept. Every cost-based power plant built by a regulated utility that operates in PJM "*distorts*" the wholesale market. Every time Jobs Ohio provides financial incentives for a new large manufacturer to locate or expand here, the wholesale power market is "*distorted*" through artificially increased demand. Undue attempts by Ohio to avoid such "*distortion*" would lead to paralysis and the loss of economic development to other states.

Nevertheless, to the extent that Sub. H.B. 6 incidentally affects the federally regulated wholesale power market, this helps consumers by lowering prices and is permissible under federal law.[3] Keeping Ohio's nuclear generation operational will put a downward pressure on prices, thus "*helping*" the buyers of power (consumers) and "*hurting*" the sellers of power (merchant gas generators). Ohio's two nuclear plants annually generate almost as much energy as is used by all of Duke Energy Ohio's consumers in Cincinnati and south-west Ohio (about 17 million MWh). Testimony before the Sub-Committee by the Brattle Group found that the increased supply from keeping Davis-Besse and Perry in operation will lower market energy and capacity rates throughout all of Ohio by $177 million, about $1.1/MWh. $177 million in market price savings for Ohio consumers is more than the approximately $153 million that the two nuclear plants will be paid from the Clean Air Fund. On this fact alone, Sub. H.B. 6 is a good deal for consumers. While reduced market prices will modestly reduce the profits earned by the natural gas generators, it will simultaneously reduce costs to the average residential consumer by approximately $0.92 per month.

[1] The Value of Energy Tax Incentives for Different Types of Energy Resources, CSR Report March 19, 2019

[2] These federal subsidies included: Credits for Investments in Clean Coal Facilities, Expensing of Oil and Gas Exploration and Development Costs, Excess of Percentage over Oil and Gas Depletion, Excess of Percentage over Cost Depletion, Amortization of Geological and Geophysical Expenditures Associated with Oil and Gas Exploration, Amortization of Air Pollution Control Facilities, 15-year Depreciation Recovery Period for Natural Gas Distribution Lines, Exceptions for Publicly Traded Partnerships with Qualified Income derived from Certain Energy-Related Activities, and Alternative Fuel Mixture Credit.

[3] "*States, of course, may regulate within the domain Congress assigned them even when their laws incidentally affect areas within FERC's domain.*" Hughes v. Talen Energy Mktg, 136 S. Ct. 1288, 1298 (2016); "*A larger supply of electricity means a lower market-clearing price, holding demand constant. But because states retain authority over power generation, a state policy that affects price only by increasing the quantity of power available for sale is not preempted by federal law.*" Elec. Power Supply Ass'n. v Star, 904 F. 3d 518, 524 (2018). "*This incidental effect on wholesale prices does not, however, amount to a regulation of the interstate wholesale electricity market that infringes on FERC's jurisdiction.*" Allco Finance Limited v. Klee, 861 F.3d 82 (2d Cir. 2017)

THERE IS NO PJM "*FREE MARKET*" THAT WILL BE HARMED BY SUBSTITUTE H.B.6

You have heard testimony that Sub. H.B. 6 would harm the otherwise free market for energy and capacity in PJM. This is not true. The PJM capacity market is a free market in only the loosest sense. On the contrary, the PJM market is heavily regulated by the federal government. PJM has had a capacity market for only 12 years. The rules that govern this so-called "*free market*" are thousands of pages long and are constantly changing as the more than 500 Voting Members of PJM seek to advantage their various interests in dozens of working groups, committees and sub-committees. The PJM stakeholder process is less like a free market and more like the United Nations.

Opponents of the bill seek to play to the general tendency of the Republican majority to favor free markets and competition. But this bill is not a choice between capitalism and socialism. It is about federal versus state regulation. There will be regulation either way.

Electricity is not like other commodities. Electricity is not like pork bellies or orange juice futures. Electricity is vital to national defense, economic security and public health. There is no substitute for electricity. And because electricity cannot be stored in quantity, there has to be an instantaneous balance of supply and demand. All of this makes electricity unique, and uniquely important. The United States Supreme Court has long recognized the important role played by the states in this field, finding that *"[T]he regulation of public utilities is one of the most important of the functions traditionally associated with the police power of the States."*[4]

[4] Ark. Elec. Co-Op v. Ark. Pub. Serv. Comm'n, 461 U.S. 375, 377 (1983).

STATES HAVE JURISDICTION OVER GENERATING FACILITIES AND SUB. H.B. 6 IS NOT PREEMPTED BY THE FEDERAL POWER ACT NOR IN VIOLATION OF THE COMMERCE CLAUSE

The Federal Power Act (FPA), 16 U.S.C. Sec. 824, was enacted in 1935. The FPA establishes a collaborative system between the states and the federal government to regulate electricity. States have exclusive jurisdiction over retail sales and "*facilities used for generation of electric energy*".[5] That is why there is an Ohio Power Siting Board that permits construction of new power plants, but there is no equivalent federal agency. The Federal Energy Regulatory Commission (FERC) has exclusive jurisdiction over the transmission of electric energy in interstate commerce and the wholesale sale of electric energy.

Sub. H.B. 6 would use Ohio's legal authority over electric generation facilities and resource planning to encourage the continued operation and construction of clean or cleaner power plants in the state.[6] FERC recognizes that states maintain the right to support their preferred generation resources in pursuit of state policy goals.[7] In my opinion, the exercise of this authority is not preempted by the FPA, or in violation of the Commerce Clause of the U.S. Constitution, so long as the state law complies with the recent U.S. Supreme Court Hughes decision[8], which it does. Sub. H.B. 6 complies with Hughes since receipt of the $9/MWh Clean Air Credit is not preconditioned on the generator's sale of capacity into a FERC-regulated capacity auction. Here is what the Supreme Court said in Hughes about promoting in-state generation.

> *"Our holding is limited: We reject Maryland's program only because it disregards an interstate wholesale rate required by FERC. We therefore need not and do not address the permissibility of various other measures States might employ to encourage development of new or clean generation, including tax incentives, land grants, direct subsidies, construction of state-owned generation facilities, or reregulation of the energy sector . Nothing in this opinion should be read*

[5] FPA Section 201 (b)(1).

[6] *"[S]tates have broad powers under state law to direct the planning and resource decisions of utilities under their jurisdiction. States may, for example, order utilities to build renewable generators themselves, or…order utilities to purchase renewable generation."* Entergy Nuclear Vt. Yankee v. Shumlin, 733 F.3d 393, 417 (2d Cir. 2013).

[7] "*States may continue to support their preferred types of resources in pursuit of state policy goals. At the same time, [FERC] has exclusive jurisdiction over wholesale rates of both subsidized and unsubsidized resources, and a statutory obligation to ensure they are just and reasonable*." Order Rejecting Proposed Tariff Revisions, Granting in Part and Denying in Part Complaint, and Instituting Proceedings Under section 206 of the federal Power Act, Docket Nos. EL18-187 et al, (June 29, 2018).

[8] Hughes v. Talen Energy Marketing, 136 S. Ct. 1288 (2016).

> *to foreclose Maryland and other States from encouraging production of new or clean generation through measures 'untethered to a generator's wholesale market participation.' So long as a State does not condition payment of funds on capacity clearing the auction, the State's program would not suffer from the fatal defect that renders Maryland's program unacceptable."*

In September 2018, a Seventh Circuit Court of Appeals decision recognized the right of Illinois to support the nuclear power plants located in that state by placing a value on zero carbon generating resources.[9] Later that same month the Second Circuit Court of Appeals likewise recognized the right of New York to support the nuclear power plants located there.[10] On April 15, 2019, the U.S. Supreme turned down challenges to those two decisions.

In the Illinois nuclear support case, the Seventh Circuit Court of Appeals summarily addressed the Commerce Clause issue in favor of Illinois. The Court reasoned that because Congress ceded jurisdiction over generating facilities to the states in the Federal Power Act, the exercise of that jurisdiction by the states does not intrude on Congress' Commerce Clause authority.[11] Moreover, because Sub. H.B. 6 is focused on clean air and public health, an area of valid state concern, it is on sound Commerce Clause footing. States have a valid interest in "*legislating on all subjects relating to the health, life and safety of their citizens"* (such as clean air) even if that "*legislation might indirectly affect the commerce of the country*."[12]

Access to the Clean Energy Fund would not be limited to only Ohio businesses. Out of state developers would be welcome. But the Fund is properly limited to in-state generation because: 1) that is the only generation

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[9] Electric Power Supply Association v. Star, 904 F.3d 518 (7th Cir. 2018).

[10] Coalition For Competitive Electricity v. Zibelman, 906 F.3d 41 (2d Cir. 2018).

[11] *"A few words about the Constitution and we are done. Plaintiffs invoke the dormant Commerce Clause and its rule that states may not discriminate against interstate transactions. Plaintiffs observe that the credits are bound to help some Illinois firms and contend that this condemns them. But this amounts to saying that the powers reserved to the states by Sec. 824(b)(1) are denied to the states by the Constitution, because state regulatory authority is limited to the state's territory. On this view, whenever Illinois, or any other state, takes some step that will increase or reduce the state's aggregate generation capacity, or affect the price of energy, then the state policy is invalid. That can't be right; it would be the end of federalism…. The commerce power belongs to Congress; the Supreme Court treats silence by Congress as preventing discriminatory state legislation. Yet Congress has not been silent about electricity: it provided in Sec. 824(b)(1) that states may regulate local generation."* Electric Power Supply Association v Star, 904 F. 3d 518 (7th Cir. 2018).

[12] Gen. Motors Corp. v. Tracy, 519 U.S. 278 (1997).

subject to the jurisdiction of Ohio; 2) only Ohio consumers pay into the Fund; and 3) Ohio has a valid interest in protecting the health of its citizens through clean air.

While Sub. H.B. 6 would not be preempted by the FPA, a facility receiving the $9/MWh Clean Air Credit (such as Beaver-Valley and Perry) would probably be considered "*subsidized*" and therefore subject to the more restrictive capacity re-pricing rules currently being developed by FERC and PJM to accommodate states that elect to pursue their own specific generation interests.[13] Sub. H.B. 6 wisely anticipates the possibility of a FERC/PJM rule change in R.C. 4928.46 and requires a recommendation from the PUCO as to how best comply.

Thank you for the opportunity to testify.

[13] Capacity Repricing or in the Alternative MOPR-Ex Proposal: Tariff Revision to Address Impacts of State Public Policies on the PJM Capacity Market, FERC Docket No. ER18-1314 (April 9, 2018); Order Rejecting Proposed Tariff Revisions, Granting in Part and Denying in Part Complaint, and Instituting Proceeding Under Section 206 of the Federal Power Act, Docket Nos. EL18-187 *et al.*, (June 29, 2018).

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