House Bill 247, House Public Utilities Committee
Opponent Testimony of Joseph Oliker
Associate General Counsel, IGS Energy
October 23, 2019

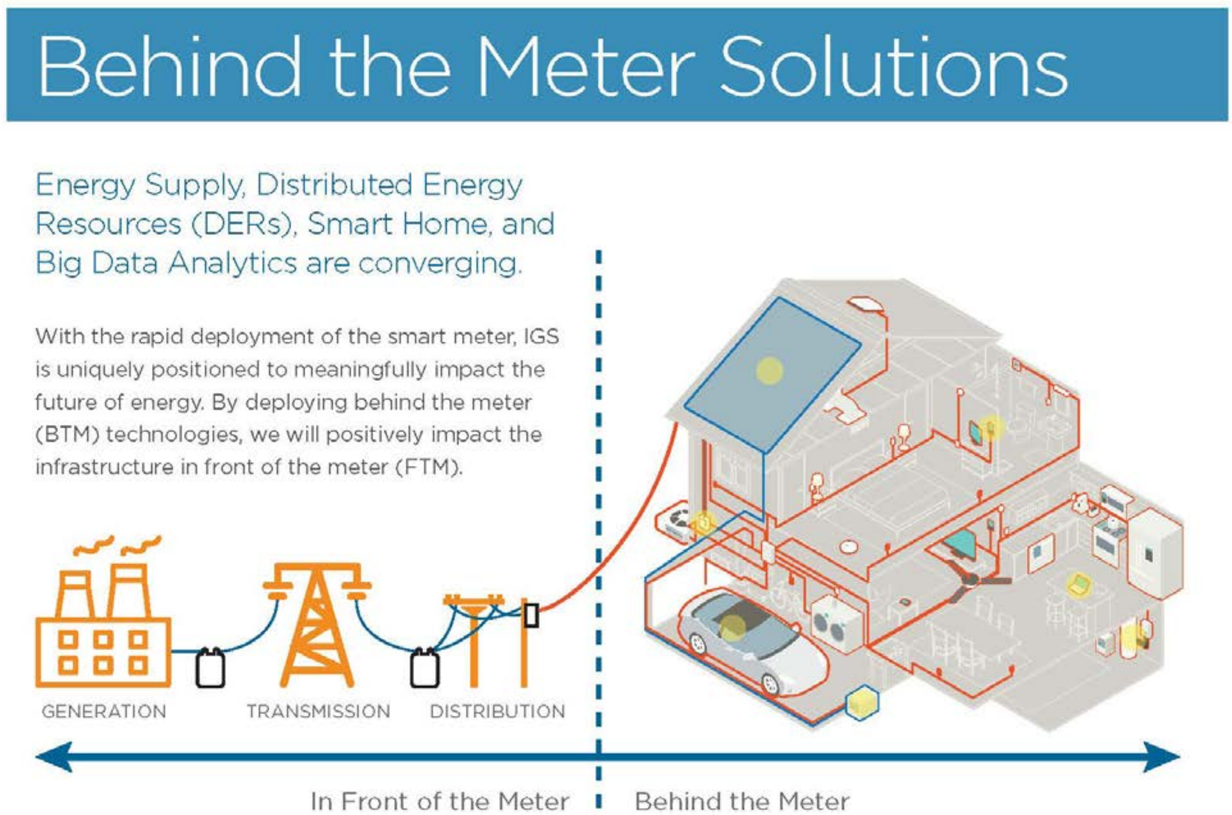
Chairman Callender, Vice Chair Wilkin, ranking member Smith and members of the House Public Utilities Committee, thank you for the opportunity to provide opponent testimony to the current version of House Bill 247 ("HB 247"). My name is Joseph Oliker, Associate General Counsel for IGS Energy.

IGS Energy is a diverse energy company that is family-owned and privately held. IGS is headquartered in Dublin, Ohio and employs more than 700 people throughout this state.

IGS directly contributes over $100 million to the economy in payroll, taxes, and local vendor expenditures annually. IGS provides over $1 million to Ohio charities and our employees volunteer over 7,000 hours per year. IGS serves over 1,000,000 retail energy customers nationwide and we conduct business in over 20 states.

IGS consistently receives accolades for its impact on Ohio. We were rated "Best Employer" by Columbus CEO Best of Business, and we were rated "Best Place to Work" by Columbus Business First.

IGS provides a range of products to customers today, from competitive generation to non-commodity products such as warranty and repair services. Many of IGS' businesses are directly focused on developing innovative behind the meter products and services. As a direct result of the pro-competitive landscape established by the General Assembly, IGS has invested hundreds of millions of dollars in Ohio



For these reasons, IGS has serious concerns with several components of HB 247, especially the proposal to permit the utilities to provide what the bill labels "customer-focused energy services or products." The bill would permit utilities to offer and subsidize these services, even though they are already available from competitive suppliers like IGS and the utilities' affiliates.

IGS supports efforts to modernize the grid and to empower customers to select innovative products that fit their needs in an ever-changing digital world. While the utilities have taken some steps to update the grid and metering systems, they still have a long way to go. Unfortunately, HB 247 does not focus on grid modernization. Rather, it is focused on permitting the utilities to provide behind the meter services.

Given our substantial investment in Ohio, we have serious concerns with the current version of HB 247.

HB 247 (Elimination of corporate separation safeguards to permit utilities to offer competitive products and non-commodity products and services)

1. **The Purpose of HB 247—Permit utilities to offer products that the competitive market is currently providing**

Current law prohibits monopoly utilities from providing competitive services and products and services other than retail electric services (commonly referred to as "non-commodity products and services"); rather, such service must be provided through a fully separated affiliate. This law exists for good reason. Allowing utilities to leverage their monopoly status in competitive markets fundamentally harms competition and ultimately harms consumers by pushing competitive suppliers out of the marketplace.

Thus, when the General Assembly restructured the energy market, it established corporate separation requirements to ensure a level playing field for competitive energy services and non-commodity products and services, just like the ones at issue here. Corporate separation required the separation of non-competitive wires service from all other services to ensure that the monopoly utility did not convey its competitive operations an advantage to the detriment of customers and competition.

For an in depth history of the purpose of corporate separation and the dangers associated with permitting a monopoly utility from offering anything other than non-competitive services, please review the attached Appendix A.

HB 247 would eliminate current corporate separation protections and permit utilities to obtain a competitive advantage for purposes of offering behind the meter services that the market is already delivering. Specifically, the Bill proposes to permit the utilities to provide "customer-focused energy services or products," which are alarmingly defined as *any* services or products provided by a utility to customers or for the benefit of customers. The proposed law provides the following non-exhaustive list of examples:

- Warranty and repair services;
- Community solar;
- Battery storage;
- Electric vehicle charging stations;

- Energy monitoring and control devices;
- Lighting controls and other smart controls;
- Microgrids;
- Energy efficiency;
- Any other technologies so classified by the public utilities commission.

These services do not relate to traditional monopoly distribution services. Rather they are optional products and services—some unrelated to electricity—that are already available in the marketplace. Additionally, the bill puzzlingly expands the definition of “smart grid” to include many of the same products and services also considered “customer-focused services or products.”

IGS is only one company in a well-diversified market, yet IGS alone already offers nearly all of the behind the services contemplated by the bill, including:

Energy Monitoring and Control Devices. IGS offers detailed energy monitoring and analysis services to customers of all classes, which enable customers to have more control over their energy bills. IGS has deployed thousands of smart hot water heaters that provide regulation service in real time to the transmission grid in order to maintain voltage. Likewise, IGS has deployed thousands of smart thermostats, which reduce total customer usage and may be utilized to reduce customer usage when the grid is under stress, without compromising comfort.

Home Warranty. IGS currently provides home warranty products to nearly 100,000 customers in Ohio alone, providing service contracts to repair HVAC, water lines, electric lines, and gas lines.

Solar. IGS is also an active developer of residential and commercial solar. Last year alone IGS invested over $200 million in customer-sited solar assets. IGS plans to invest even more this year.

Energy Efficiency and Lighting. IGS provides customized energy efficiency and lighting solutions to customers that fit their business needs.

Electric Vehicles. IGS Labs is developing EV smart charging products and services. This is one of many behind the meter products and services under development by IGS Labs.

Battery Storage. IGS and other competitors are developing products and services as standalone products and in conjunction with renewable energy resources.

The competitive market is well situated to meet customer demands of the future. It provides opportunities for Ohioans to take advantage of these additional products and services, without burdening others with the cost.

IGS has concerns regarding several components of HB 247. Passage of the Bill without serious modification would shake our confidence in the regulatory and legislative landscape in this state and cause IGS to reconsider future investment in Ohio.

2. HB 247 Permits Utilities to Subsidize Product Offerings

Despite assertions by the proponents of this bill, HB 247 does not simply permit the utilities to compete on "a level playing field." Utilities can already offer competitive services through their competitive affiliates like everyone else. Instead, the real purpose of the bill is to allow the utilities to require its captive customers to subsidize the cost of competitive services through distribution rates. Thus, the bill would tilt the playing field against the competitive market and increase customers' electric bills.

The bill provides several avenues to deploy "customer-focused energy services or products." Each avenue would be subsidized and have little to no safeguards.

First, the bill permits utilities to amend their corporate separation plan to permit the offering of such products and services. Under this option, utilities are prohibited from collecting the *incremental direct costs* associated with such optional offerings in their base distribution rates (Lines 828-832). That means the utilities are permitted to recover *indirect costs* through distribution rates. Moreover, the bill strikes from current law the prohibition against extending a competitive advantage or preference to a portion of the business offering non-electric services, in this case customer-focused energy services or products (Lines 798-799). It should be very concerning that HB 247 is **removing** customer safeguards.

Second, whatever safeguards the bill contains regarding the provision of competitive services, the bill permits utilities to completely disregard these very protections to the extent that a customer-focused energy service or product has been authorized by the Commission as part of an electric security plan ("ESP") or another section of Ohio law (Lines 880-884).

To the extent that customer-focused energy services are approved in an ESP, the utilities could recover direct and indirect costs from all customers. Indeed, the bill specifically provides that these services are eligible for distribution service cost recovery under R.C. 4928.143(B)(2)(h). Indeed, **Lines 607-634** would allow utilities to implement "Provisions regarding the *utility's distribution service*, including . . .(v) Deployment of smart grid technology; (vi) Provision of *customer-focused energy services or products* . . . providing for the utility's recovery of costs, including lost revenue, shared savings, and avoided costs, and a just and reasonable rate of return . . . ." Thus, contrary to the utilities' claim that the bill would provide a level playing field, the bill would permit utilities to subsidize their product offering. Providing guaranteed cost recovery for competitive services is a throwback to the antiquated and outdated utility business model that existed prior to restructuring in 1999.

If there is any doubt regarding the subsidization of utility product offerings, this is further confirmed by Lines 481-482, which eliminates from state policy the prohibition against anticompetitive subsidies flowing from a noncompetitive retail electric service to a non-commodity product or service. Why would you want to eliminate this provision, unless there was a desire for a utility to receive anti-competitive subsidies?

The clear intent of the bill is to eliminate corporate separation safeguards and to permit utilities to enter new markets and subsidize their product offerings on the backs of all distribution customers. HB 247 would knock down core pillars that ensure a functional market for energy services within this state. There is simply no good reason to remove long-standing customer safeguards to permit the utilities to provide behind the meter services when the utilities' affiliates can and do currently compete in this space on a true level playing field.

3. Commentary Regarding Specific Services

The utilities have claimed that there is a desire from customers to receive these services that the market has not met. First, if that were the case, one would have expected customers to provide proponent testimony in support of the bill. They did not. Second, to the extent customers want these products, all of them are available through the competitive market.

a. Warranty and Repair Services

One of the apparent purposes of HB 247 is to permit utilities to provide warranty and repair services to customers. These products do not even relate to electricity. Non-commodity services may include appliance repair, HVAC repair, and various line extensions (water, gas, or electric) on the customer premises.

But the bill does not define what services the utilities may provide; therefore, there are no limitations on the type of warranty and repair services that may be authorized. The General Assembly must recognize the harmful impacts associated with introducing a subsidized product in an already established market. Because the definition of "customer-focused energy services or products" enables an endless list of offerings, the scope of harm is not limited to companies in the energy industry.

Additionally, many of the utilities already have affiliates that provide warranty and repair services without the assistance of ratepayer dollars.[1] This demonstrates that the current corporate separation requirements are working just as designed. The utilities, through an affiliate, are offering products and services with their dollars, just like every other competitor in the market. This is a true level playing field.

b. Community Solar

The provision in the bill related to community solar is somewhat of a misnomer. That term typically refers to "virtual net metering," which is a process of treating an in front of the meter renewable resource as if it were behind the meter for purposes of calculating the bill of individual subscribers. Since the bill makes no attempt to fix Ohio's broken net metering policy, which undercompensates customer-sited renewable resources, it is difficult to determine what the bill seeks to accomplish other than to permit the utilities to build and market solar.

[1] https://www.duke-energy.com/home-services/strikestop.

The Ohio utilities, however, already have affiliates that compete to develop renewable projects.[2] There is no good reason to permit the utilities to offer these products.

c. Electric Vehicle Charging Stations

IGS supports electric vehicle adoption and is developing EV-charging service options for customers. But, as a practical matter, there has been little EV adoption in Ohio to date. For example, last year there were only 4,500 EVs purchased in Ohio, with only a total of 14,000 EVs in the state. There is no need for the utilities to provide EV charging stations to serve this population.

Moreover, it does not make sense to permit utilities to enter this space when a $11.5 million in incentives for EV charging station development are in the process of being distributed as a result of the Volkswagen settlement.[3] A more measured approach would wait to see if the market deploys sufficient infrastructure to keep up with demand.

It appears that the market is poised to meet demand. Just last week, Ford announced that it "is offering its all-electric vehicle customers North America's largest electric vehicle public charging network, with more than 12,000 places to charge, including fast charging, and more than 35,000 charge plugs . . . ."[4] Within the last six months, General Motors and Bechtel announced their intention to construct a network of fast-charging stations across the United States. And Tesla has plans to further expand its national charging network. Thus, the market is already building charging stations, without saddling distribution customers with additional non-bypassable charges.

d. Energy Efficiency and Lighting Controls

---

[2] https://www.duke-energy.com/annual-report/_/media/pdfs/our-company/investors/de-annual-reports/2018/2018-duke-energy-annual-report.pdf *see* p. 15. *See also* https://www.aes.com/investors/press-releases/press-release-details/2017/AES-and-AIMCo-Agree-to-Acquire-sPower-the-Largest-Independent-Solar-Developer-in-the-United-States-from-Fir-Tree-Partners/default.aspx. https://aep.com/about/businesses/aeponsitepartners.

[3] https://epa.ohio.gov/Portals/42/documents/VW/DMTF-EV-Charging-Stakeholder-Mtg.pdf

[4] https://media.ford.com/content/fordmedia/fna/us/en/news/2019/10/17/ford-introduces-north-americas-largest-electric-vehicle-charting-network.html

HB 6 just gutted the energy efficiency portfolio standards, implicitly suggesting that these measures would be better provided through the competitive market rather than bloated programs funded by all customers. It defies reason that the General Assembly would then turn around and pass legislation that could actually increase ratepayer funded energy efficiency measures.

Making matters worse, there are no safeguards with respect to the size or cost of the energy efficiency programs the utilities could implement, given that they would be authorized within the context of an electric security plan as opposed to R.C. 4928.66. Keep in mind that within an ESP case, the only cap on energy efficiency spending is whether the otherwise applicable outcome is more favorable than what would occur in a fully market-based paradigm. Given that energy efficiency programs—even prior to House Bill 6—were required to be "cost effective," it can be expected that utilities will file robust portfolio plans as if HB 6 never happened.

e. Microgrids

A microgrid is localized power network constructed around a distributed generation resource, which permits the local grid to operate independently and autonomously from the traditional distribution grid. Due to efficiencies in distributed generation, microgrid products are available from several competitive suppliers. While utilities may have a role in integrating microgrids into the larger distribution grid, there is no reason for the utilities to own distributed generation resources connected to a microgrid. These resources should be constructed by the competitive market and paid for by customers that benefit from the them rather than monopoly distribution rates.

f. Energy Monitoring and Control Devices and Batteries

Utility affiliates and competitive suppliers are already constructing battery storage resources and offering a menu of services to customers.[5] The bill would tilt the competitive playing field against the market and permit

[5] https://www.aes.com/investors/press-releases/press-release-details/2017/Siemens-and-AES-Join-Forces-to-Create-Fluence-a-New-Global-Energy-Storage-Technology-Company/default.aspx; *see also* https://www.duke-energy.com/renewable-energy/energy-storage#targetText=Duke%20Energy%20is%20a%20leader,leading%20edge%20of%20microgrid%20solutions.

utilities to subsidize battery products and services. Consequently, the bill would discourage new market entry into a growing industry.

4. **Are there any components of the bill that relate to economic development?**

There are a few isolated components that could, with appropriate safeguards, encourage new customers to relocate in Ohio. For example, the bill would permit utilities to automatically recover the cost of constructing line extensions and substations for new customers. Today, absent a “reasonable arrangement,” a new customer is typically required to pay for a significant amount of the distribution-related upgrades necessary to commence electric service. Arguably, this component of the bill would make it less expensive for a business to locate in Ohio. IGS does not necessarily oppose this portion of the bill but it is worth mentioning there are no limitations on what projects the utilities can undertake.

Summary

IGS supports economic development, competition, and efforts to modernize the distribution grid. But this bill does little to promote those goals. There is simply no good reason to permit the utilities to leverage their monopoly assets to subsidize products and services behind the meter, particularly when such products are already offered by the competitive market and the utilities’ own affiliates. Thank you for the opportunity to submit testimony regarding the current version of HB 247. With any remaining time, I would be happy to answer any questions you may have.

APPENDIX A

Historical Context for "Corporate Separation" and "Unbundling" Non-Competitive Services from Other Services from Utility Rates

In order to understand how HB 247 would impact the energy landscape in Ohio, it is important to consider the reasons for the current paradigm. When the General Assembly restructured the energy market, it established corporate separation requirements to ensure a level playing field for competitive energy services and products and services unrelated to electricity.

This was achieved through a two step process. First, competitive and non-competitive services were "unbundled", meaning that total customer electric rates were separated into competitive (generation) and non-competitive (distribution) portions. Customers were given the opportunity to compare different offers for competitive services and to select the provider of their choosing.

Second, the historically vertically integrated utilities were required to divest their competitive businesses (unregulated business) from the monopoly non-competitive business. Utilities were required to transfer any competitive businesses—whether they relate to energy or some other endeavor—to a separate affiliate. In a nut shell, this ensured that monopoly utilities did not extend a competitive advantage to their competitive services, for example by recovering the cost of competitive services from captive distribution customers.

Even when a utility transfers its competitive businesses to an affiliate, that does not ameliorate the risk that the utility will seek to use its regulated operations for the benefit of its unregulated affiliate. Therefore, utilities are required to file formal corporate separation plans that: (1) prohibit utilities from offering competitive products; and (2) contain specific rules detailing the manner in which a monopoly utility may interact with its affiliates, in order to ensure that the affiliate does not receive a competitive advantage by virtue of that relationship to a monopoly utility.

Corporate Separation—In Economic Literature

Economists and Professors have discussed the concept of corporate separation in depth for decades. But, from a high level, they have concluded that functional competitive markets do not permit monopoly utilities to provide competitive services. When they are permitted to provide both monopoly-based and competitive services, there is a great risk that they will leverage their monopoly assets to convey a competitive advantage to any internal business or division that provides the competitive service.

There are numerous ways that this may occur. Many of the potential opportunities of monopolist to exploit their captive customer base for unregulated profits and the detriment of competition. These pitfalls are discussed in the excerpts below, taken from articles and books describing core principles necessary for a functional market for competitive services.

As far back as the 1987, in *Why Regulated Firms Should be Kept Out of Unregulated Markets*, Timothy Brenner discussed the risk and opportunity for a monopoly utility to recover competitive costs through non-competitive regulated rates, which allows the utility to undercut competitors, increase market share, and maximize its own profits:

> Suppose that the monopolist can *allocate costs of supplying other markets to its regulated business*. *If so, rates for the regulated product will rise under cost-of-service regulation.* The prices in the other markets, however, will generally be set by competition among the other firms in those markets. *If the regulated firm can allocate some of the costs of providing service in those unregulated markets to the regulated market, the profits in the unregulated markets will rise.* The direct effect will be that the price of the regulated product rises, with the attendant profits appearing in the operations of the regulated firm in the unregulated markets.
>
> To see this direct effect, let us return to the hot dog monopolist. Suppose the monopolist enters the sausage business, which is assumed not regulated. The competitive price of sausages in the market is 45 cents. Assume that the expense for the pork used to make sausages can be assigned to the hot dog business. In other words, the hot dog regulator cannot tell whether the firm's purchase of pork went into the making of hot dogs or into the

making of sausages. The hot dog manufacturer has the incentive to allocate pork used to make sausages to the hot dog side of the business, up to 25 cents per hot dog. At that point, the regulated price of hot dogs rises to $1. Profits are taken through selling sausages at 45 cents, while the apparent costs are lower due to the shifting of pork costs to the production of hot dogs.

[B]y writing off costs of its competitive services against the regulated sector the regulated firm faces lower costs of supplying competitive markets. This may result in an increase in its share of the competitive market over what it would have been had the costs not been misallocated. At the margin, this may result in the displacement of more efficient capacity of unaffiliated firms by less efficient capacity of the regulated firm. In the extreme, more efficient suppliers of the competitive product may be excluded altogether. This ability arises not from the regulated firm's efficiencies, but because its costs may be borne by customers of its regulated product through cost misallocation.[6]

Mr. Brenner concerns have been echoed by several other well-respected economists. As Dr. Jonathon Lesser explained, "it is important to ensure that the non-regulated cost of a product are not tagged with regulated costs. Cross-subsidization crates two problems. First, it unfairly increases the price of regulated goods to captive customers, and regulators would be unable to determine if the price of the regulated item reflects costs other than those involved with its production."[7] Such "cross-subsidization prevents unregulated firms from competing with the regulated firm with regards to the unregulated product, because those other firms are forced to set their prices without the benefit of a cross-subsidy."[8]

Likewise, during the federal process of restructuring undertaken in response to FERC Order 888, the Federal Trade Commission noted that

[6] Brenner, *Why Regulated Firms Should be Kept Out of Unregulated Markets: Understanding the Divestiture in United States v. AT&(and)T*, 32 Antitrust Bull. at 759 (1987). Attached in supporting documents.

[7] Lesser and Giacchino, *Fundamentals of Energy Regulation* at 196, Public Utilities Reports, Inc. (2013).

[8] *Id*.

"Preventing Discrimination or Cost Shifting by a Regulated Monopolist Is Difficult." Indeed, it further identified that:

> A monopolist whose rate of return is regulated has an *incentive to evade the regulatory constraint in order to earn a higher profit. Its participation in an unregulated market may give it the means to do so, either by discriminating against its competitors in the unregulated market or by shifting costs between the regulated and unregulated markets.*
>
> The discrimination strategy involves complementary products. The monopolist controls others' access to its regulated product in ways that permit it to earn supra competitive returns in its own operations involving the unregulated complement."
>
> The cross subsidization or cost shifting strategy involves inputs used for both regulated and unregulated products. Costs of the shared inputs, which in the electric power industry might include scheduling and general overhead, are assigned to the regulated business to justify higher cost-based rates there. This shifting distorts competition and produces inefficiencies in the unregulated business as well. Controlling the discrimination and cost-shifting strategies with monitoring and regulation is difficult. They can be defeated most effectively by preventing the regulated monopolist from entering the unregulated business, thus eliminating its ability to distort competition in the unregulated market.[9]

As is relevant to HB 247, the monopoly utilities have have several different "cost-based" recovery mechanisms, such as base distribution rates and various riders. This provides an opportunity allocate the cost of providing competitive services—either direct or indirect costs, such as overhead, marketing, and IT—to non-competitive cost-based rate mechanism.

---

[9] ***Competition and Consumer Protection Perspectives on Electric Power Regulatory Reform, Staff Report: Competition and Consumer Protection Perspectives on Electric Power Regulatory Reform*** Federal Trade Commission (2000) (emphasis added). *See* https://www.ftc.gov/reports/competition-consumer-protection-perspectives-electric-power-regulatory-reform#N_43_

Even the diligent regulator seeking to prevent this outcome is at a disadvantage, given the nature of the ratemaking and regulatory process. There is no punishment for misallocation of costs other than a denial of cost recovery. Therefore, a utility the no incentive to correctly assign costs. Rather, the opposite is true because allocating competitive costs to non-competitive cost recovery mechanisms increases the profits of the unregulated entity and permits it to undercut competitors to the disadvantage of non-subsidized competitors.

Based upon the risk that a monopoly utility will subsidize its competitive products, most restructured states have required the legal/physical separation of competitive businesses from the monopoly. It is generally accepted in the energy industry that "unbundling" of incumbent monopoly rates alone does not sufficiently ensure a level playing field. Rather, physical and structural separation of competitive businesses from the monopoly entity is required to avoid cross-subsidization of unregulated services by regulated services, as well as to avoid the potential for discriminatory treatment of other market participants:

> Vertical separation of potentially competitive segments (e.g. generation, marketing and retail supply) from segments that will continue to be regulated (distribution, transmission, system operations) either structurally (through divestiture) or functionally (with internal "Chinese" walls or "ring fencing" separating affiliates within the same corporation). These changes are thought to be necessary to guard against cross-subsidization of competitive businesses from regulated businesses and discriminatory policies affecting access to distribution and transmission networks upon which all competitive suppliers depend.[10]

According to Hunt, separation of competitive and non-competitive businesses is necessary due to the inherent conflict of interest that exists for a monopoly provider of distribution service. Thus, a key aim is to:

> To eliminate as far as possible any *conflict of interest* between the competitive entities (generators and retailers) and the

[10] Joskow, *Lessons Learned From Electricity Market Liberalization* at 12, The Energy Journal (2008). Attached in supporting documents.

> providers of the essential facilities (transmission, system operations, and distribution). This includes eliminating *opportunities to discriminate, as well as cross subsidies* between regulated and unregulated activities.[11]

Indeed, "When competitive and regulated activities are in the same company (or affiliated companies) the concern is cross-subsidization of the competitive activity by the regulated activity."[12] Or the use its "competitively useful information about customers to its retailing subsidiary that it does not provide to competing retailers.[13]

In summary, failure to separate competitive from non-competitive function results in excessive prices for customers and destroys competition. The monopolist enterprise has an incentive to leverage its regulated operations to reap unregulated profits. The monopolist achieves this result in several ways:

- Discrimination against competitors by limiting access to information or facilities
  - For example, utilization of customer-specific information to market products and services while erecting mechanical, logistical, or financial barriers for competitors to access the same information
  - For example, utilizing the ratepayer funded utility billing system to invoice and collect for good and services while prohibiting competitors equal access to do the same for like services
  - Marketing renewables to new customers into the service territory without any consideration of competitive offers
  - Tying the development of a substation to procuring additional unregulated products.
- Cross-subsidization of unregulated products and services

---

[11] Hunt, *Making Competition Work in Electricity* at 38, John Wiley & Sons (2002) (emphasis added) (*see* http://regulationbodyofknowledge.org/wp-content/uploads/2013/03/Hunt_Making_Competition_Work.pdf)

[12] Hunt, *Making Competition Work in Electricity* at 59-60 (2002).

[13] Hunt, *Making Competition Work in Electricity* at 220-221 (2002).

- Collecting through monopoly distribution rates the overhead, administrative, and capital costs associated with offering unregulated products and services.
- Example, labor, utility bill, advertising

Permitting monopoly utilities to offer competitive products has the tendency to result in excessive prices and creates barriers to development and sustainability of the market. Therefore, structural separation of non-competitive and competitive services is the most effective way to provide a level playing field.