OHIO ENERGY GROUP

– Turning Energy Into Jobs –

Interested Party Testimony of
Michael Kurtz
On Behalf of the Ohio Energy Group
Before the Senate Energy and Public Utilities Committee
SB 346
December 1, 2020

Chairman Wilson, Ranking Member Williams, Vice Chair McColley and distinguished Members of the Committee. Thank you for the opportunity to provide testimony today.

My name is Michael 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 27 members spend more than $1 billion annually on gas and electricity and we provide more than 55,000 good paying direct jobs in Ohio. Depending on individual state policy decisions, energy costs can vary widely among even neighboring states. Keeping energy costs low in Ohio is very important to the national and global competitiveness of Ohio's energy intensive manufacturers.

I am testifying today as an interested party.

OEG was an active participant in the Legislative process that ultimately resulted in HB 6. We were as surprised as anyone to learn about the allegations of wrongdoing. But despite its origins, much of HB 6 remains good policy. HB 6 had two primary outcomes:

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First, HB 6 implemented a $9/MWh subsidy payment to the Davis-Besse and Perry nuclear plants ($150 million per year) and to six large solar plants ($20 million per year). These $9/MWh subsidy payments last for the seven-year period 2021-2027 and total approximately $1.2 billion. The nuclear and large solar subsidy payments are capped at $0.85 per month for residential customers and $2,400 per month for large users

Second, HB 6 eliminated subsidy payments for energy efficiency and peak demand reduction (EE/PDR) programs as of the end of 2020, and scaled back and then ended after 2026 subsidy payments for renewable generation through the Renewable Portfolio Standard (RPS) mandates. These pre-HB 6 subsidy payments were not capped.

Over the six-year period 2014-2019 the pre-HB 6 EE/PDR subsidies cost consumers $1.627 Billion. Over the same period the pre-HB 6 RPS subsidies cost consumers $320 million. Therefore, the total pre-HB 6 EE/PDR and RPS subsidy payments over that six years were $1.947 Billion. For 2019 alone, the pre-HB 6 EE/PDR and RPS subsidies were $367 million, or more than double the new nuclear and large solar subsidies of $170 million.

In May 2020, LSC concluded that by replacing the very costly uncapped pre-HB 6 EE/PDR and RPS subsidies with the less costly capped nuclear, large solar, and scaled back RPS subsidies, HB 6 will actually save all residential, commercial and industrial consumers $2.357 Billion over the 2020-2030 period.

An earlier LSC analysis is instructive in estimating the HB 6 impact on individual residential customers. LSC determined that as of April 2019, the pre-HB 6 EE/PDR and RPS subsidies cost the average residential customer $4.68 per month.[1] Of this $4.68, about $3.84 was for EE/PDR which will completely go away next year under HB 6, and about $0.84 was for RPS which will be scaled back under HB 6. Therefore, under HB 6, each month residential customers will continue to pay an RPS charge of about $0.84 and will pay a new nuclear and large solar charge of $0.85, but they will stop paying $3.84 for EE/PDR. This results in a net saving for residential customers

[1] R-133-0948-2

of $2.15 per month, or approximately $25.8 per year. There are 4.2 million residential customers of Ohio's six investor owned electric utilities.

Large industrial customers will have much more competitive rates as a result of HB 6. Below is a chart showing the OVEC, RPS, EE/PDR and nuclear/large solar costs for a mid-sized industrial customer on the AEP system pre and post HB 6. For the sample customer the savings are $313,532 per year.

20 MW Industrial Manufacturing on AEP System[2]

2019 Pre-HB 6

OVEC	RPS	EE/PDR	Nuclear/Large Solar
$87,393	$47,216	$225,723	$0.0
Total 2019 Cost $360,332			

2021 Post-HB 6

OVEC	RPS	EE/PDR	Nuclear/Large Solar
$18,000	$0.00	$0.00	$28,800
Total 2021 Cost $46,800			

HB 6 Annual Savings $313,532

While there is justifiable anger regarding recent revelations about how H.B. 6 was enacted, that anger should not be directed at Ohio consumers.

A targeted reform of only the nuclear subsidy provisions, while maintaining the other good policy aspects of H.B. 6, may be appropriate. Some supporters of full repeal correctly argue that the current law audit provisions could be enhanced to ensure that the two nuclear plants actually need a $150 million annual subsidy to remain in

[2] Billing determinants and rates for this analysis are attached to my testimony.

operation. At the conclusion of this Testimony I will outline a suggested revision to R.C Sec. 3706.61 regarding this issue.

Legal Background

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 (FERC/PJM) to regulate electricity. States have exclusive jurisdiction over retail sales and "*facilities used for generation of electric energy.*" 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.

There are three components of electricity supply: distribution, transmission and generation (capacity and energy). Distribution comprises the small wires and transformers on local roads. All states regulate distribution the same way— cost-of-service rate base/rate of return. Distribution utilities get a return of and on their distribution investment, plus recovery of reasonable expenses. FERC/PJM also regulate transmission through cost-of-service rate base/rate of return. Transmission owners get a return of and on their transmission investment, plus recovery of reasonable expenses. Many states (Indiana, Kentucky, Virginia, West Virginia, Georgia, Alabama, Florida) also regulate generation through cost-of-service rate base/rate of return. The rate of return on invested equity capital authorized by all states and FERC for cost-based distribution, transmission or generation service is generally 9%-10%.

However, Ohio (along with 12 other PJM states) has turned over the regulation of generation pricing to FERC/PJM. FERC/PJM regulate wholesale generation pricing through the establishment of very complex marginal cost-based energy and capacity markets. Marginal cost regulation pays all generation suppliers the same amount regardless of their individual cost-of-service. The rules for these federally regulated wholesale energy and capacity markets are thousands of pages and are consistently changing.

The owners of Davis-Besse and Perry and other nuclear plants in PJM claim that the federally regulated wholesale energy and capacity markets unreasonably pay them the same as dirty coal, gas or oil power plants by not properly valuing resilient base load, zero carbon nuclear resources. The HB 6 $150 million annual nuclear subsidy for seven years was intended at least in part to address this alleged flaw.

Illinois and New Jersey both recently enacted nuclear bailout legislation to address this same alleged flaw in the FERC/PJM wholesale energy and capacity markets. Those actions were both upheld by the federal courts as not being in conflict with the Federal Power Act or Commerce Clause.[3]

Renewable Portfolio Standard

A Renewable Portfolio Standard (RPS) basically requires that consumers buy Renewable Energy Certificates (RECs) for a certain amount of the energy they consume. Each MWh of wind or solar generation produces one REC. This provides an additional revenue stream to wind and solar developers. FERC generally considers this to be a subsidy. Ohio has had an RPS since 2008.

HB 6 reduced and then eliminated Ohio's RPS mandate after 2026. But if HB 6 is repealed in full and the old law snaps back, in 2027 and each year thereafter, 12.5% (including a 0.5% solar portion) of all energy purchased by customers of investor owned electric utilities (customers of municipal utilities and cooperative utilities were exempt) will have to be paired with RECs. RECs are bought and sold in organized markets just like any other commodity. From 2014 (when the RPS was 2.5%) to 2019 (when the RPS was 5.5%) the annual average cost to Ohio consumers of RPS compliance was $53 million. The majority of RECs currently supplied in Ohio (about 78%) are from out-of-state resources.

Other than a global reduction in CO2 which benefits all humans and an impossible to quantify reduction in energy prices across the entire 13-state PJM region, Ohio consumers get no direct benefit from having to subsidize

[3] Electric Power Supply Association v. Star, 904 F.3d 518 (7th Cir. 2018); Coalition For Competitive Electricity v. Zibelman, 906 F.3d 41 (2d Cir. 2018).

out-of-state wind and solar developers through the purchase of their RECs. Many of Ohio's neighboring states have no RPS mandate, including Indiana, Kentucky, Virginia, West Virginia, Georgia, Alabama and Florida.

Even without an Ohio RPS, the federal government already heavily subsidizes renewable generation through generous Investment Tax Credits for solar (currently 26%) and Production Tax Credits for wind (currently $15/MWh).

Energy Efficiency/Peak Demand Reduction Mandates

The EE/PDR mandates have been part of the law since 2008. These mandates require that utilities buy an escalating amount energy efficiency and demand reduction savings from participating ratepayers (discounts for more efficient motors or lighting retrofits, rebates for more efficient refrigerators, "free" energy efficient lightbulbs that come in the mail, etc.) using money paid by non-participating ratepayers.

Back in 2008, load was growing and the utilities owned power plants. The original rationale for EE/PDR was to defer the need for new utility owned power plants, thus lowering costs to all consumers. But the utilities no longer own power plants. Generation supply has since been turned over to FERC/PJM and the competitive wholesale markets. The original rationale for using ratepayer money to buy energy savings from other ratepayers has long since passed.

The EE/PDR mandates are very expensive. For the period 2014-2019, the EE/PDR costs were $1,627,154,216 ($271 million per year). These were the costs necessary to achieve the mandated 2014-2019 1% per year reduction in energy usage. If H.B. 6 is repealed, then the old law will snap back and the mandated energy savings will increase to 2% per year for the period 2021 to 2027. Some believe that it is reasonable to assume that a doubling of the mandate will double the costs. I disagree. I believe that the cost increase will be non-linear and will more than double. The low hanging fruit has already been picked. Hunting for new energy efficiency savings when usage is already depressed due to COVID will be difficult and costly.

Most people don't understand how the energy efficiency mandates work in practice. Here is an example. Assume that nine members of this Committee and the Chairman are each charged 50 cents by their utility to raise $5 for energy efficiency. After utility shared savings (profit margin) and administrative overhead assume that 80% or $4.0 remains to be spent on actual programs. Assume that the $4.0 was spent on an LED light bulb that was sent to the Chairman. He was charged 50 cents, but he received a subsidized LED light bulb worth $4. A pretty good deal for the Chairman. He will probably save money on his future electric bills. But what did the other nine members of the Committee get? Perhaps a societal benefit of less pollution. Perhaps an impossible to measure reduction in wholesale energy prices across all of PJM's thirteen states. But the other nine members received nothing of tangible value.

The proponents of full repeal argue that the reinstatement of the EE/PDR mandates will actually save *participating* consumers more money than the cost to *non-participating* customers. Their math is questionable.

How much money will participating customers (like the Chairman) save? It depends on your assumptions to the following questions: would the Chairman have bought an LED lightbulb without a ratepayer subsidy (free rider question), what type of lightbulb will be replaced by the subsidized LED (incandescent, CFL or another LED), how long will the subsidized lightbulb sit in the closet before being used, how many hours per day will the subsidized lightbulb operate, what is the assumed future price of energy that will be avoided, what discount rate should be applied to the projected savings over the life of the subsidized lightbulb? Different assumptions yield wildly different results.

OVEC

A secondary, but controversial, issue addressed in HB 6 is OVEC. OVEC is comprised of two mid-1950s vintage coal-fired power plants located in Indiana and Ohio. OVEC is owned by a consortium of utilities in Ohio, Indiana, Michigan, Kentucky and West Virginia, including AEP Ohio, Duke Energy Ohio and Dayton Power & Light. OVEC was originally created to serve the massive energy requirements of the Department of Energy's gaseous diffusion plant in Portsmouth, Ohio as part of this Country's nuclear defense efforts. Although old, the OVEC plants

have new environmental control equipment (ESPs for particulates, SCRs for NOX and scrubbers for SO2). But the OVEC units are currently not profitable. All of the OVEC energy and capacity is sold into the PJM wholesale markets, but the OVEC costs (primarily new debt acquired for scrubbers in 2013-2104) exceed its revenue.

HB 6 guaranteed the Ohio utility owners of OVEC recovery of net losses (and the flow-through of any profits) through 2030. HB 6 capped cost recovery at $1.5 per month for residential customers and $1,500 per month for large users. But HB 6 did not impose OVEC costs on consumers. OVEC costs were already being recovered by the utilities pursuant to prior PUCO Orders, and those Orders have been affirmed by the Ohio Supreme Court. Therefore, repealing HB 6 will not make OVEC costs go away.

Keeping Ohio's Two Nuclear Plants In Operation At The Lowest Cost To Consumers Through A More Comprehensive OAQDA and PUCO Financial Needs Assessment

OEG opposes the full repeal of H.B. 6 since full repeal will increase costs to consumers by reinstating costly EE/PDR and RPS mandates. OEG takes no position on whether Ohio's two nuclear plants should be subsidized. Despite the current controversy surrounding HB 6, prior policy makers in the House, Senate and Executive Branch did believe that saving the two nuclear plants was appropriate.

If current policy makers decide that Ohio's nuclear power plants should continue to be subsidized to help ensure their continued operation, then it may be appropriate to more fully verify that the level of subsidy is justified by financial need. The determination of financial need would be through enhanced PUCO and Ohio Air Quality Development Authority (OAQDA) oversight.

Under current law (RC Sec. 3706.61), each year the PUCO is required to conduct a "retrospective management and financial review" of both the owner or operator of the nuclear plants as well as the nuclear plants themselves.

Then, OAQDA in consultation with the PUCO "may cease or reduce payments for nuclear resource credits" (e.g. the $9/MWh subsidy payment) if one of four triggering events occur.[4]

None of the four triggering events is financial need. So the first change to existing law would be to explicitly make financial need a triggering event for lowering the subsidy payment. The second legislative change would be to define financial need. Below, we define financial need to be breakeven operations with no profit margin. This would be the lowest level of ratepayer subsidy necessary to keep the nuclear plants from retiring.

- Financial need would be defined to mean breakeven operations with no profit margin. Payments to Davis-Besse and Perry would be capped at no more than $9/MWh to cover only their actual and prudent costs with no profit margin. This is effectively a zero percent rate of return on invested equity, in contrast to the 9%-10% return typically authorized on utility investments across the country and at FERC.
- Payments can be less than $9/MWh if that amount is not needed for either of the nuclear plants to break even (no profit). This means that the annual nuclear subsidy cannot exceed $150 million, but may be less.
- In its annual retrospective management and financial review, OAQDA and the PUCO would examine forecasted revenue from all sources (including all credits and incentives received, accrued or related to zero emission CO2 production) and all reasonable and prudent expenses. Reasonable and prudent expenses cannot include lobbying costs, political or charitable donations, management bonuses or incentive compensation. In other words, no ratepayer subsidy can cover these costs.
- Determination of break-even done on an individual plant basis based on its specific revenues, expenses and capital structure. This will help ensure that the reduced cost structure from the prior FES bankruptcy is

[4] The four triggering events are: (1) FERC or NRC has established a monetary benefit or other incentive payment to continue the resource's commercial operation; (2) the plants are no longer fueled by nuclear power or the nuclear plant operator no longer maintains its principal place of business and a substantial presence in Ohio; (3) the plant owner applies to decommission the plant; or (4) the market price index of forecasted energy and capacity revenue exceeds the $46/MWh strike price, in which case the $9/MWh payment shall be reduced by an equivalent amount.

reflected and passed through to consumers. Perry (1987) is nine years newer than Davis-Besse (1978), is more efficient (by about $3/MWh) and may require less subsidy payments to break even.

- The plant owner may experience a loss if the $9/MWh capped subsidy payment is not sufficient to break even.
- Reasonable expenses to include depreciation. Recovery of depreciation is always allowed in regulated distribution, transmission and generation rates. Depreciation is a non-cash expense. Recovery of depreciation ensures positive cash flow, but no profit. This will incentivize the plant owners to continue in operation, thus preserving jobs, tax base and zero carbon generation.

  Specific statutory language to accomplish this suggestion is attached to my testimony.

Thank you or the opportunity to testify.

Sec. 3706.61. (A) In each year beginning in 2021 and ending in 2027, the public utilities commission shall, not later than the first day of May of each of those years, conduct a retrospective management and financial review of the owner or operator of a qualifying nuclear resource and any such resource that receives payments for nuclear resource credits under section 3706.55 of the Revised Code. In doing so, the commission may retain consultants and advisors to perform all or any portion of the annual reviews, the cost of which shall be paid, at the direction of the Ohio air quality development authority, by the treasurer of state from the nuclear generation fund in accordance with section 3706.55 of the Revised Code.

(B) Any owner or operator subject to a review under division (A) of this section shall~~may~~, for purposes of the review, provide the commission or the commission's consultants or advisors with any information the commission requests~~owner or operator chooses~~. The owner or operator shall promptly and fully respond to any document, information, data, or other request that may be directed to its attention by the commission or the commission's consultants or advisors for the purpose of the review. Any material failure to timely and fully respond shall result in suspension of further receipt of payments for nuclear resource credits under section 3706.55 of the Revised Code until the failure is cured to the satisfaction of the commission.

(C) The commission shall submit a report summarizing the findings of each annual review to the president and minority leader of the senate, the speaker and minority leader of the house of representatives, and the Ohio air quality development authority, and shall make the report publicly available, provided that the report shall not reveal any confidential or proprietary information. The submission shall include a copy of the owner's or operator's own certified annual audit that was obtained during the review performed under this section.

(D) In consultation with the commission, the Ohio air quality development authority shall consider the findings of the review and shall~~may~~ cease or reduce payments for nuclear resource credits under section 3706.55 of the Revised Code if the authority determines any of the following:

(1) That the federal energy regulatory commission or the nuclear regulatory commission has established a monetary benefit or other incentive payment to continue the resource's commercial operation;

(2) That either requirement under division (A) or (B)(2) of section 3706.43 of the Revised Code is no longer being met;

(3) That the resource's owner or operator applies, before May 1, 2027, to decommission the resource;

(4) That, for the purpose of ensuring that the funding for nuclear resource credits remains reasonable, the market price index exceeds the strike price on the first day of June in the year in which the report is submitted, in which case the authority shall apply the credit price adjustment for the twelve-month period that begins on that day and ends the thirty-first day of May, or, for 2027 , for the seven-month period that begins on that day and ends the thirty-first day of December;~~.~~

(5) That, for the purpose of ensuring that the funding for nuclear resource credits helps to maintain the economic viability of the qualifying nuclear resource at the lowest cost to consumers, the payment of nuclear resource credits shall be limited to the amount necessary to increase the net income or profit margin of the qualifying nuclear facility from a negative amount to zero for the annual review period. In determining whether any qualifying nuclear resource operated with no net income or profit margin, all

revenue received or accrued from all sources, and only reasonable and prudent expenses, shall be considered. Reasonable and prudent expenses cannot include lobbying costs, political or charitable donations, management bonuses or incentive compensation. Reasonable and prudent expenses shall include depreciation.

(E) (1) If the authority determines it necessary to make reductions under division (D) of this section, the commission shall do all of the following, as necessary:

(a) Reduce the revenue requirement under division (A)(1) (a) of section 3706.46 of the Revised Code;

(b) Except when the authority has applied the credit price adjustment under division (D)(4) of this section, reduce the price of a nuclear resource credit under section 3706.45 of the Revised Code, in accordance with a reduced revenue requirement;

(c) Reduce the charge or charges under section 3706.46 of the Revised Code, to conform with a reduced revenue requirement;

(d) Adjust the percentages under section 3706 .53 of the Revised Code in accordance with a reduced revenue requirement.

(2) Any revisions made by the commission under division (E)(1) of this section shall be made through a process that the commission shall determine is not for an increase in any rate, joint rate, toll, classification, charge, or rental, notwithstanding anything to the contrary in Title XLIX of the Revised Code.

(F) If the payments for nuclear resource credits are suspended or ceased under this section, the commission shall instruct the electric distribution utilities to accordingly suspend or cease billing and collecting customer charges under section 3706.46 of the Revised Code.

(G) Chapter 4903. of the Revised Code shall not apply to this section. Sec. 3706.63. Not later than January 1, 2020, the Ohio air quality development authority shall adopt rules under Chapter 119. of the Revised Code that are necessary to implement sections 3706.40 to 3706.65 of the Revised Code.

Billing Determinants and AEP Rates

20 MW

70% Load Factor

122,640,000 kWh per year

2019 Pre-HB 6

OVEC Charge $0.0007126/kWh

RPS 5.5% at $7/MWh

EE/PDR January through July 2010 $0.89/KW and credit of ($0.0003566)/kWh;
August through December $0.79/KW and $0.0005533/kWh

No Nuclear/Large Solar Charge

2020 Post-HB 6

OVEC capped at $1,500/month

No RPS for large users (above 45 million KWh annually)

EE/PDR phased out by end of 2020

Nuclear/Large Solar capped at $2,400/month