

OHIO ENERGY GROUP

– Turning Energy Into Jobs –

**Interested Party Testimony of
Michael Kurtz
On Behalf of the Ohio Energy Group
Before the House Select Committee on Energy Policy and Oversight
HB 738 and HB 746
September 23, 2020**

Chairman Hoops, Ranking Member Leland, Vice Chair Abrams 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 recent allegations of wrongdoing. But despite its origins, much of HB 6 remains good policy. HB 6 had two primary outcomes:

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

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Cargill, Incorporated
Charter Steel
Elyria Foundry
Fiat Chrysler Automobile US LLC
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GE Aviation
General Motors LLC
Greif, Inc.
Howmet Aerospace Inc.
JSW Steel (USA) Inc.
Johns Manville (Berkshire Hathaway)
Martin Marietta Magnesia Specialties, LLC
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North Star BlueScope Steel, LLC
Praxair Inc.
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Ohio Energy Group
36 E. Seventh St., Suite 1510
Cincinnati, Ohio 45202
Ph: 513.421.2255
Fax: 513.421.2764
www.OhioEnergyGroup.com

General Counsel

Michael L. Kurtz
Boehm, Kurtz & Lowry
513.421.2255

President

Joe Price
330-471-7059

Vice President

Greg Long
513-425-4728

Treasurer

Eric Hoegger
952-984-4025

For Further Information Contact

Denny Larr, Governmental Relations
Larr Policy Consulting
614-824-3201



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.

In PUCO Chairman Randazzo's September 16, 2020 Testimony to this Committee, he calculated that over the six-year period 2014-2019 the pre-HB 6 EE/PDR subsidies cost consumers \$1.627 Billion. Chairman Randazzo also testified that 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-year period was \$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 6.² 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

² The breakout between EE/PDR and RPS was done based on the 2019 data on Attachments C and D to Chairman Randazzo's September 16, 2020 Testimony.

of \$2.15 per month, or approximately \$25.80 per year. There are 4.2 million residential customers of Ohio's six investor-owned electric utilities.

Bottom line: HB 6 will save all consumers \$2.357 Billion over 2020-2030, and will save 4.2 million individual residential customers approximately \$25.80 per year beginning next year.

While there is justifiable anger regarding recent revelations about how HB 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 HB 6, may be appropriate. Some supporters of HB 738 and HB 746 correctly argue that the current law audit provisions could be enhanced to ensure that the two nuclear plants need a \$150 million annual subsidy to remain in operation. PUCO Chairman Randazzo addressed this concern in his Testimony last week. At the conclusion of this Testimony I will outline a suggested mechanism to supplement existing law 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 costs. 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 Exelon Corp. owns four nuclear power plants in Illinois, two of which receive a subsidy payment and two do not. On August 27, 2020 Exelon gave notice to PJM that the two non-subsidized plants would retire prematurely by November 2021.

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

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).

produces one REC. This provides an additional revenue stream to wind and solar developers. FERC 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. As noted previously, as Chairman Randazzo testified last week, 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. A full repeal of HB 6 will result in even higher annual compliance costs, as the annual targets will continue to escalate at twice the pace of current law. 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 out-of-state wind and solar developers through the purchase of RECs. Many of Ohio's neighboring states have no RPS mandate, including Indiana, Kentucky, Tennessee, Virginia, West Virginia, Georgia, Alabama and Florida.

Recent information from the Ohio Power Siting Board demonstrates that the HB 6 reduction then elimination of Ohio's RPS mandate has not hindered the development of utility scale wind and solar generation. As of August 2020, a total of 12,351 MW of solar and 1,789 MW of wind facilities in Ohio have started the interconnection process as a necessary prerequisite to actual construction. This is due in part to the generous Investment Tax Credits for solar (currently 26%) and Production Tax Credits for wind (currently \$15/MWh) already provided by the Federal Government.

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 of 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. If utilities estimate that they will achieve the required savings, then they can receive an added profit called shared savings. But if the utilities estimate that they will not achieve the required savings, then the law requires that the Commission shall assess a forfeiture (penalty) on the utility. Suffice it to say that the utilities will achieve, or at least estimate that they will achieve, the required savings.

Back in 2008, load (demand for electricity) was growing and the utilities owned power plants. The original rationale for EE/PDR was to defer the need for new utility-built power plants, thus lowering costs to all consumers. But the utilities no longer own or build 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. But this is controversial. A whole industry has grown up around selling energy efficiency to utilities.

The EE/PDR mandates are very expensive. According to Chairman Randazzo, 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 HB 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 \$5.00 for energy efficiency. After utility shared savings (profit margin) and administrative overhead assume that

80% or \$4.00 remains to be spent on actual programs. Assume that the \$4.00 was spent on an LED light bulb that was sent to Chairman Hoops. He was charged 50 cents, but he received a subsidized LED light bulb worth \$4.00. 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.

Non-participating consumers (like the nine members of this Committee) will clearly lose money from full repeal. Reinstatement of the EE/PDR mandates will require them to pay a very substantial tangible cost, but they will receive no tangible benefit.

But how much money will participating customers (like Chairman Hoops) save? It depends on your assumptions to the following questions: would Chairman Hoops 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?

In 2014-2019 utility shared savings (profit margin) were \$408 million. Because the utility shared savings depend on assumed savings, the utilities have a profit incentive to over-estimate. However, as stated earlier, if the utilities estimate under compliance, then they shall be penalized. Bottom line: the cost to non-participating consumers is substantial and real; but the savings to participating customers is very difficult to quantify.

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 \$1.50 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.

OVEC is not an Ohio problem. It is a regional problem. And there is no good answer. But repealing HB 6 will not fix OVEC.

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

OEG opposes the full repeal of HB 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. The prior Legislative record contained Testimony from the Brattle Group that the two nuclear plants provide 4,300 direct and indirect jobs, \$510 million in annual Ohio GDP, \$30 million in annual state and local taxes and enough zero carbon energy to power about 1.4 million

homes. In addition, the premature retirement of the two nuclear plants could necessitate transmission upgrades which would be an added cost to consumers in Northern Ohio.

In Chairman Randazzo's Testimony last week, he recognized (although he did not take a position one way or another) that modifying current law to more clearly or comprehensively reduce the \$9/MWh credit and corresponding customer charges based on a financial need assessment could be accomplished by making relatively modest adjustments to current law. We agree with the Chairman. 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 for the PUCO to more fully verify that the level of subsidy is needed.

The following is a potential targeted adjustment of only the nuclear subsidy provisions of HB 6 that may make sense:

- 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.
- Annual filing at PUCO of all 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. Plant owner is required to maximize revenue before any state subsidy is available. Reasonable and prudent expenses cannot include lobbying costs, political or charitable donations, management bonuses or incentive compensation.
- 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

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 annual forecast to be trued-up to reflect actual revenues and expenses. This is the way FERC regulates transmission rates. The plant owner may experience a loss if the \$9/MWh capped subsidy payment is not sufficient to break even.
- Maximum term seven years, same as HB 6. Nuclear plant owner can opt-out of Ohio subsidy funding for either plant at any time during the seven-year term for any reason. The subsidy payment would then end.
- Reasonable expenses to include depreciation. Depreciable life based on the longer of the projected economic useful life of each plant or end of its NRC license date. Perry's NRC license expires in 2026 and Davis-Besse in 2037. 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 and tax base.

Thank you or the opportunity to testify.