



**BEFORE THE SENATE ENERGY & PUBLIC UTILITIES COMMITTEE
SENATOR BOB PETERSON, CHAIRMAN**

**TESTIMONY
OF
KIM BOJKO
PARTNER, CARPENTER LIPPS & LELAND
OMA ENERGY COUNSEL**

FEBRUARY 2, 2021

Mr. Chairman and members of the Senate Energy and Public Utilities Committee, my name is Kim Bojko. I am a partner with the law firm Carpenter, Lipps, and Leland, where I specialize in public utility law. I also serve as energy counsel to both The Ohio Manufacturers' Association (OMA) and the OMA Energy Group. I appreciate the opportunity to present proponent testimony on Senate Bill 10 (SB 10).

The OMA represents the manufacturing sector of Ohio. We boast approximately 1,300 members – of all sizes. It is impossible to competitively operate a modern manufacturing facility without affordable and reliable power. Our membership includes many of the largest, most sophisticated energy users in the state. Some of our members consume the same amount of electricity as a medium-sized city. In short, energy is very important to Ohio's manufacturing competitiveness.

The OMA was an opponent of House Bill 6 (HB 6). OMA and its members testified numerous times in opposition to the anti-consumer and anti-competitive provisions of the bill now tied to the pending bribery investigation by the Southern District of Ohio's U.S. Prosecutor's Office.

During the waning days of the 133rd General Assembly, the OMA testified on several different pieces of legislation that addressed the repeal of HB 6. Last year, the OMA supported then Representative Romanchuk's House Bill 772 as the most comprehensive approach to address the problems presented by HB 6.

Today, the OMA continues to push for a legislative package that would repeal HB 6 in a manner that protects customers and markets. Then and now we suggest a repeal bill that contains the following elements:

- Repeal the Clean Air Program and rider created by HB 6 to subsidize the nuclear power plants and select renewable energy projects, which publicly available data, including from Energy Harbor itself, proves are not needed.
- Repeal the OVEC rider created by HB 6 that continues to subsidize the two old coal plants, including one in Indiana, owned by a consortium of energy companies known as the Ohio Valley Electric Corporation and prevent the PUCO from enacting a new OVEC rider without explicit approval from the General Assembly.
- Repeal the decoupling mechanism in HB 6 that benefits FirstEnergy by rewarding it with unearned income at the expense of customers. A repeal package should also require FirstEnergy to immediately refund the full amount of those ill-gotten gains to customers.

- Require the PUCO and the Ohio Air Quality Development Authority to eliminate or rescind any mechanism, charge, rule, or order enacted, authorized, or issued to implement an anti-market provision of HB 6.

The OMA also presented opponent testimony to the Significantly Excessive Earnings Test (SEET) that was included in the last General Assembly's operating budget bill, House Bill 166 (HB 166).

We are pleased SB 10 repeals both the SEET revision and the decoupling provisions and requires utilities to refund these ill-gotten gains to customers, the victims of these provisions. We think SB 10 is a good start to rebalance the relationship between customers and utilities. However, we would urge the Senate to push harder to protect customers and markets by including all the above-mentioned recommendations now in SB 10, and not wait for subsequent legislation.

Decoupling

In general, a decoupling mechanism separates a utility's revenue from the volume of electricity that it delivers. Consequently, a decoupling mechanism ensures that a utility's revenue target is reached, regardless of how much electricity is sold.

Traditional decoupling mechanisms were included in Senate Bill 221 (SB 221) as a tool to help make the utilities whole from reduced sales resulting from state-mandated energy efficiency programs. Decoupling is used to remove the disincentive in order to promote energy efficiency. While legislative proponents touted HB 6 as the law that would lower customers' bills by eliminating energy efficiency mandates and the costs associated therewith, decoupling mechanisms enable the utilities to charge customers for lost distribution revenue associated with energy efficiency programs that no longer exist. Since these mandated utility-administered energy efficiency programs were repealed in HB 6 without repealing corresponding decoupling riders, customers were left taxed without any benefit. We applaud SB 10's inclusion of a repeal of the decoupling mechanisms associated with non-existent energy efficiency programs.

The HB 6 created decoupling mechanism goes far beyond traditional decoupling, benefitting only the FirstEnergy utilities to the tune of \$102 million in 2021 alone (an increase from \$17 million in 2020). The HB 6 decoupling mechanism has zero correlation with energy efficiency, demand reduction, or anything else of value to customers or a legitimate policy goal. It was devised pure and simple to provide a windfall to the FirstEnergy utilities' regulated monopolies.

Then CEO Chuck Jones famously told investors months after passage of HB 6 that the decoupling mechanism made FirstEnergy "somewhat recession proof." As Senator Romanchuk pointed out in his testimony, FirstEnergy is guaranteed to receive its 2018

distribution revenue, which is \$978 million annually, regardless of consumer usage for the foreseeable future. FirstEnergy will also receive an additional \$66.5 million per year in “lost distribution” revenue, above and beyond the \$978 million in base distribution revenue. By making this change, FirstEnergy successfully transfers risk to its customers.

Characteristic	Typical Decoupling Mechanism	HB 6 Decoupling Mechanism
Utility revenue recovered from ratepayers	Average sales year	Very high sales year
Overcharges	Credited to customers	Unlikely to be credited to customers
Revenue requirement reevaluation	Next scheduled distribution rate case	No scheduled distribution rate case (could be in perpetuity)
Joint policy initiatives	Energy efficiency programs, distributed generation programs	None
Effected utilities	Available to all state-regulated electric distribution utilities	Just FirstEnergy utilities
Regulatory process allowing customer engagement	Yes	No

Table 1. Typical Decoupling vs H.B. 6 Decoupling Design Features

I’ve incorporated a table in my testimony contrasting the HB 6 created decoupling mechanism from traditional or typical decoupling mechanisms. Additionally, I have attached an OMA commissioned analysis by energy consultant RunnerStone that outlines in depth decoupling and the provisions in HB 6.

Significantly Excessive Earnings Test

The original SEET was contained in comprehensive energy reform legislation (SB 221) more than a decade ago. The SEET is the lynchpin of SB 221’s consumer rate protections, prohibiting utilities from charging rates that generate “significantly excessive earnings.” Profits earned by a utility above the “significantly excessive” threshold must be refunded to customers.

In the years since enactment, the PUCO has twice defined greater than 17% return on equity as the threshold to trigger SEET customer refunds (OMA and numerous other parties contested that level as overly generous). Regrettably for customers, the Ohio SEET profit threshold is greater than in many competitor states and has allowed Ohio’s electric utilities to reap greater profits from captive customers than in other states where return on equity is typically much lower.

The SEET applies to utility profits stemming from Electric Security Plan (ESP) cases (EPSs were also a mechanism created in SB 221). ESPs are filed by electric distribution utilities to provide a variety of services in exchange for distribution charges on customer bills.

Customers are increasingly unified that these two ratemaking provisions are anti-competitive and unfair and bad for consumers and Ohio's economy.

Prior to HB 166 of the 133rd General Assembly, the PUCO was required to perform SEET on a utility-by-utility basis to determine if individual utilities over earned. Under the test, if a utility over earned, the utility refunded the excess earnings to its customers.

But HB 166 changed the SEET and required the PUCO to consider the total earned return on equity of all three distribution utilities of FirstEnergy collectively when applying the SEET.

With the HB 166 change, if one distribution utility in a family of distribution utilities is over earning, it will offset an affiliated distribution utility that is not as profitable. The bill allowed FirstEnergy to shield a utility that is excessively earning by offsetting those excessive profits with an affiliated utility that is not as profitable, allowing the parent company to retain profits that are otherwise required to be given back to customers. This eliminated a customer protection that was enacted as part of Ohio's ESP ratemaking statutes.

The ramification is that FirstEnergy does not have to refund monies to customers for one of its utilities if that utility is over earning.

This provision did nothing to protect customers. Instead, it protected only the FirstEnergy utilities at the expense of their customers. We fully support its inclusion in SB 10.

Conclusion

While SB 10 is a good first step in the right direction, the Senate would do well to consider including the additional enumerated provisions to help protect customers and markets from the indefensible policies enshrined in HB 6.

We thank Senator Romanchuk for sponsoring this important legislation to protect and grow Ohio manufacturing.

Thank you. I would be happy to answer any questions.



MEMORANDUM

Date: September 17, 2020

To: The Ohio Manufacturers' Association

From: John Seryak, PE and Peter Worley (RunnerStone, LLC)

RE: H.B. 6's Decoupling Provision – A Primer on Decoupling and How H.B. 6 Decoupling Benefits FirstEnergy by Deviating from Best Practices

H.B. 6 has well-known provisions that affect Ohio's nuclear power plants, coal power plants, select solar power plants, and energy efficiency. Less well-known is a confusing decoupling provision. Fortunately, FirstEnergy's CEO put the effect of the provision in plain language for its investors:

“essentially it takes about one-third of our company and I think makes it somewhat recession-proof”¹

As a result of this decoupling provision, FirstEnergy could collect about \$355 million in unearned revenue through 2024. Ratepayers will incur higher electricity costs with no associated benefits. Moreover, a unilateral ruling from the PUCO could extend FirstEnergy's decoupling at the utility's discretion. This could, for example, cost FirstEnergy customers an additional \$400 million if extended from 2025 through 2030.²

Decoupling can be a legitimate policy when carefully implemented with best practices and coupled to other state policy objectives. However, H.B. 6's decoupling provision does not follow best practices, nor does it advance any state policy goal. The table below shows a comparison of the design features of a typical decoupling mechanism and those of FirstEnergy's HB6-enabled decoupling mechanism.

¹ <https://www.utilitydive.com/news/firstenergy-nears-proposal-to-decouple-ohio-utility-revenues-electricity-c/566610/>

² Memorandum to The Ohio Manufacturers' Association, “H.B. 6 Decoupling Provision - \$355 Million for FirstEnergy through 2024, Possibly Millions More”, [https://ohiomfg.informz.net/ohiomfg/data/images/-%20OMA%20MEMO%20-%20HB%206%20Decoupling%20-%20FINAL%20\(Aug.%2014,%202020\).pdf](https://ohiomfg.informz.net/ohiomfg/data/images/-%20OMA%20MEMO%20-%20HB%206%20Decoupling%20-%20FINAL%20(Aug.%2014,%202020).pdf).

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Table 1. Typical Decoupling vs H.B. 6 Decoupling Design Features

In the remainder of this memo we review the policy behind decoupling and further describe differences between H.B. 6’s decoupling provision and typical decoupling provisions.

Decoupling Basics

Electric utility monopolies are motivated to increase their profits, like any business. However, electric utility monopolies do not compete for new customers or with new products to increase profits. Instead, monopoly electric utilities receive a government-administered return on and of its investments. Overtime, this traditional model has incited utilities to overbuild to increase its financial return. The more a utility builds, the greater its total return.

The utility recovers its costs and return - the sum of which is called the revenue requirement - through charges on electricity sold (kWh), charges on customer peak power needs (kW), and customer service charges set in rate cases which have been historically held every 3 to 10 years. However, because customer kWh and kW are not constant in any given year, a utility will collect more or less than its revenue requirement in years between rate cases. A utility would prefer to over-collect between rate cases. This dynamic incites utilities to actively discourage customer energy-efficiency and on-site generation. By driving up customer consumption between rate cases, utilities can increase their profits. As a result, utility cultures and practices can form that actively discourage customer energy-efficiency and on-site generation adoption. Utilities can actively discourage customer energy management through their electric tariff designs, interconnection policies, and account management culture.

Simply put, traditional electric utility monopolies are incited to overbuild, oversell, and discourage customer energy management and choice.

Importantly, competitive markets have been an effective policy antidote for the distorted economic incentives of monopolies. Competitive markets have been employed for power generation. However, they have not been employed for electric distribution companies (the “wires” companies).



While electric distribution utilities were originally competitive during the very early years of the industry, today, it is typical for distribution companies to be government-granted monopolies.

Absent readily competitive markets for “wires” companies, some states have implemented decoupling to combat utility overbuilding and overselling. Traditional decoupling requires a utility to true-up its collected revenue between rate cases to its revenue requirement. As a result, where true decoupling is in place, the utility is not incented to over-sell electricity between rate cases, because it would have to refund customers for over-collection. Constraining energy sales thus also limits overbuilding, which is driven by sales forecasts. And, if sales for some reason are too low, the utility is also protected. Subsequently, decoupling has several goals:

1. Protects customers and automatically issues customer rate decreases or credits between rate cases in case of over-collection;
2. Allows distribution utilities to recover prudent costs to provide distribution service;
3. Encourages the distribution utility to be more cost-efficient with their operational costs and capital costs; and
4. Reduces the distribution utility’s opposition to customer choice around energy efficiency and on-site generation.

Decoupling policies are often jointly implemented with state policies to encourage energy efficiency and on-site generation. Sometimes these proactive policies are desired, especially where local utilities have strong anti-efficiency and anti-customer choice cultures. Common sense and recent experience tell us that an anti-customer choice culture persists within Ohio’s utilities.

H.B. 6’s Decoupling Provision Design Features

H.B. 6’s decoupling provision is missing or distorts important design features of a typical decoupling mechanism and will not have the intended effect of a true decoupling policy. In this sense, it is decoupling in name only. In effect, it is a semi-permanent over-charge policy that allows FirstEnergy’s utilities to profit. And, currently, it is only FirstEnergy’s utilities that profit.

There are best practices when designing decoupling. FirstEnergy’s decoupling does not follow those best practices.

Very High Utility Sales and Customer Overcharges

A typical decoupling mechanism pegs a utilities revenue requirement to a typical year of capital and operational expenses. H.B. 6 severely distorted this approach by instead prescribing FirstEnergy’s revenue requirement to the revenue it received in a peak sales year, 2018. Note, it was not based on the revenue requirement for 2018, which is based on expected costs, but, instead, it was based on the actual revenue FirstEnergy received. FirstEnergy had higher sales in 2018 as compared to other years, partially due to abnormally high temperatures which increased customer consumption. By prescribing 2018 as a representative year, this inflates the revenue requirement, which increases customer bills with no associated benefits.



Moreover, FirstEnergy's decoupling mechanism includes no revenue adjustments, and its resulting significantly excessive profits are unlikely to be capped. Typically, there are adjustments required for situations such as unseasonable weather, major changes in number of customers, or economic recession. Such adjustments are to mitigate the risk to customers of the distribution utility receiving windfall profits from circumstances that make an actual year much different than the representative or "test" year. These adjustments are in place to handle the very circumstance we are facing in 2020. COVID-19 has significantly reduced customer consumption and peak usage than a typical year, causing the distribution utility to receive less revenue. Yet, since FirstEnergy's decoupling plan includes no adjustments, FirstEnergy can receive greater profit due to the economic downturn, which increases customer bills with no associated benefits. Despite the economic downturn, the H.B. 6 decoupling mechanism will allow FirstEnergy to receive the same record revenue that it received in 2018.

Additionally, unusual revenue was also included in the H.B. 6 decoupling provision. Typically, decoupling establishes the revenue requirement based on typical operational and capital costs. FirstEnergy's decoupling provision also included so-called "lost revenue" from energy efficiency programs from the past as revenue they also need in the future. This so-called lost revenue equals approximately \$66 million per year, potentially in perpetuity. Put proverbially, FirstEnergy is having its cake and eating it too.

Moreover, a near simultaneous law change governing FirstEnergy's significantly excessive profits will allow FirstEnergy utilities to keep profits that previously may have been refunded to customers.³

Joint Policy Initiatives

As discussed, decoupling is often paired by lawmakers with policies that advance customer energy-efficiency or customer-sited distributed generation. FirstEnergy CEO Chuck Jones even referenced energy efficiency to justify this decoupling provision, saying it "Allows us to continue to promote energy efficiency with our customers so that they can get the benefit of that without impacting our base revenues."⁴ This is a curious statement as H.B. 6 simultaneously ended the requirement for Ohio's distribution utilities to achieve energy efficiency savings. And, FirstEnergy proactively suspended the bulk of their energy-efficiency programs early, in January 2020, even though they were under no requirement to do so. The other Ohio utilities, which have not implemented the H.B. 6 decoupling mechanism, offered efficiency programs through 2020. Furthermore, FirstEnergy also has taken no steps to offer non-mandated efficiency programs in 2020 as Jones' statement may suggest.

The H.B. 6 decoupling provision furthers none of Ohio's policy goals.

³ Memorandum to the Ohio Manufacturers' Association Energy Group, "Impact of the 2019 FirstEnergy SEET Amendment", <https://www.ohiomfg.com/wp-content/uploads/OMA-Memos-SEET-Combined-CLL-and-RS-Aug-20-2020.pdf>.

⁴ <https://www.utilitydive.com/news/firstenergy-nears-proposal-to-decouple-ohio-utility-revenues-electricity-c/566610/>



Effected Utilities

H.B. 6's decoupling provision does not apply statewide. H.B. 6 included some eligibility limitations to the decoupling provision that have constrained its application to other utilities. For example, the provision states that revenue recovery be "recovered pursuant to an approved electric security plan under section 4928.143 of the Revised Code, as of the twelve-month period ending on December 31, 2018." As it happens, only FirstEnergy has implemented a decoupling mechanism and is receiving decoupling revenues based on the H.B. 6 provision. Duke is not eligible for the decoupling mechanism and AEP Ohio and DP&L have not yet implemented an H.B. 6 decoupling mechanism (although AEP Ohio has tried).

Regulatory Process with Customer Engagement

Typically, the details of a decoupling mechanism will be determined within a regulatory process that allows customer intervention. H.B. 6's decoupling provision prescribed considerable detail without customer input. The design process was non-transparent and non-representative.

Finally, the PUCO issued a ruling on its own accord after the passage of H.B. 6, which gives FirstEnergy discretion on when it next files a distribution rate case. H.B. 6's decoupling provision's term is limited to its current distribution rate case. Thus, the PUCO's ruling could allow the H.B. 6 decoupling provision to extend in perpetuity. We expect that FirstEnergy will do so, so long as decoupling is more financially beneficial to it than what could be achieved with a new rate case.