

Senate Public Utilities Committee

Testimony in Opposition to SB 128
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Dynegy Opponent Testimony – SB 128

Chairman Beagle, Vice Chair LaRose and Ranking Member Williams, my name is Hank Jones and I am the Chief Commercial Officer and an Executive Vice President at Dynegy Inc. I extend you my thanks for the opportunity to provide testimony on Senate Bill 128, the FirstEnergy nuclear subsidy bill.

Dynegy Summary

Before making comments specific to the proposed legislation, if you'll permit me I would like to offer the committee a refresher on who Dynegy is and how we fit into Ohio's energy market.

Dynegy is the second largest independent power producer in the United States with more than 31,000 MW of generation at 50 power plants, enough to power more than 25 million households. Dynegy owns generation assets in 12 states and is involved in nearly every organized wholesale energy market in the United States (including the California ISO, ERCOT (Texas), MISO, PJM, NYISO and ISO-NE; excluding only SPP). Additionally, Dynegy's retail operation serves more than 1 million customers nationwide. Dynegy employs more than 2,800 employees across the country, including nearly 1,200 union members.

Dynegy is the largest generation owner of any kind in Ohio. No utility and no other independent power producer owns more generation in Ohio than we do. The Dynegy fleet in Ohio includes 10 power plants totaling more than 6,200 MW and includes both coal and natural gas fueled units. Dynegy's Ohio sited generation produces enough power to supply electricity to more than 5 million homes. Dynegy's Ohio retail operation, Dynegy Energy Services, supplies approximately 8 million MWh of power to more than 250,000 retail customers in Ohio. Dynegy employs more than 450 Ohio-based employees at our power plants located throughout the state and at our retail offices located in Cincinnati. Last year, Dynegy received the JD Power award for "Highest in Residential Customer Satisfaction with Retail Electric Service in Ohio."

Dynegy is also committed to the environment. Dynegy's goal is to recycle 100% of its coal ash for beneficial reuse by 2020. In 2017 at Miami Fort we expect to recycle 99% of our coal ash and at Zimmer we plan to recycle 76%. As we've transformed our fleet, we've reduced our GHG intensity by approximately 25% over the past few years. At the same time, SO₂ and NO_x intensity has declined by 48% and 17%, respectively.

We've accomplished all of this through private investment – not by reaching into the wallets of captive ratepayers or through the imposition of expensive non-bypassable mandates.

Turning to the proposed legislation that this Committee has been tasked with considering, I would like to share the reasons for Dynegy's opposition to this special fee.

State of Ohio Marketplace

Ohio has successfully made the nearly complete transition from a fully regulated state to a well-functioning re-structured state. Dynegy entered Ohio in 2015 when we closed on the nearly \$3 billion transaction to acquire the Duke Energy Ohio generation portfolio. As a result of Ohio's move to a restructured market, Duke made the decision to exit the competitive generation business and Dynegy determined that Ohio was the kind of state we should make investments in. Ohio's support of competitive energy markets, access to low cost natural gas, and the diversity of fuel resources we could acquire here helped inform our investment decision.

In the past two years, Dynegy has invested more than \$300 million to upgrade and improve the operational efficiency of our Ohio plants. In addition, we have hired 45 people as Dynegy employees, not contractors, to assist in our operations and growth in Ohio bringing the total number of Dynegy employees in Ohio to more than 450, not including the more than 500 temporary workers who assist our team during plant maintenance. It is my hope that these facts and my willingness to testify before you today reflect our commitment to Ohio, our intention to remain an active market participant, and our willingness to invest shareholder dollars where it makes sense to do so.

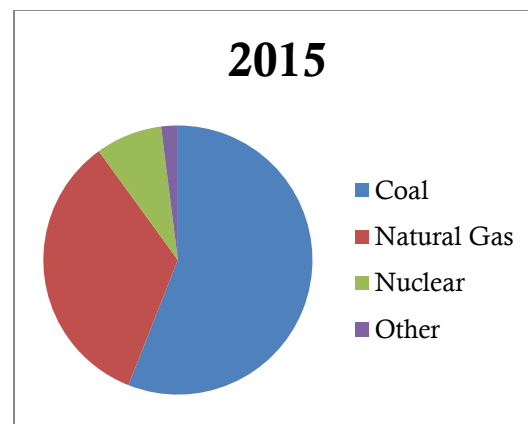
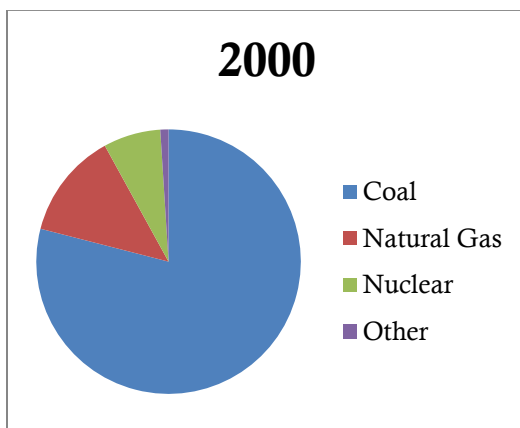
Since 2010, Marcellus and Utica gas resources have fundamentally changed the energy landscape, particularly in PJM. While I would like to think companies and governments can predict things as monumental as the shale gas revolution we know that simply isn't true.

Senate Bill 128 or the Zero Emissions Nuclear credit bill ("ZEN bill") would provide an enormous subsidy to one nuclear operator for units that are no longer economic to operate. The only plants that qualify for these subsidies are owned by FirstEnergy. The reasons being offered for why you should support this subsidy include fuel diversity, job retention, price stability, and economic development, among others. The problem with each of those arguments is none of them stand up to serious scrutiny.

Fuel Diversity

As the owner of both coal and natural gas fueled generation units in Ohio we understand and have built our business around fuel diversity. We also take note of the fact the Ohio's generation portfolio is actually becoming more diverse, as shown below:

	2000	2015
Coal	79%	56%
Natural Gas	13%	34%
Nuclear	7%	8%
Other	1%	2%



What these charts show is this: the shale revolution and the competitive market resulted in a more diverse fuel supply than Ohio had in the days of the vertically integrated utility model.

Job Retention

While I am certainly sympathetic to the employees and communities impacted by large employers who reduce workforce or close their facilities, that problem isn't unique to power plants. Communities and employees can be impacted by the closure of any number of industries and they are not able, nor should they, come to you and say "subsidize us and keep our factory open." Our economy will not grow and prosper by artificially keeping alive business that can no longer compete in the marketplace. Certainly, that has been the case throughout American history. We are constantly evolving and recreating our businesses and occupations. Were that not so, we'd still have buggy whip and ice box manufacturers and tele-type and elevator operators. As a country, we did not subsidize those industries and jobs and

Ohio ratepayers shouldn't be required to subsidize nuclear units that can no longer effectively compete in the marketplace.

Further, it is not clear whether these nuclear plants will even close. FirstEnergy has said they won't be the long-term operator of the plants, which would suggest that some other company may buy those assets. Whether that sale is from FirstEnergy Solutions or out of a bankruptcy proceeding isn't yet clear. What is clear is that this bill supposes that a pre-packaged bankruptcy is coming and ensures that the buyer of the plants will receive the ZEN subsidy in full once they acquire the assets. The proposed legislation would drive up the price FirstEnergy Solutions or the bankruptcy trustee receives from a buyer in the bankruptcy proceeding. The future buyer may have bought the assets without the subsidy just at a lower price. The proposed subsidy clearly distorts the market price for these assets and negatively impacts jobs at other, economic power plants and at plants being developed by others.

Regardless, if the plants remain in operation under a different owner the jobs, tax revenue and zero emissions benefits continue at no cost to Ohio. A change in the uniform worn by the employees shouldn't come with a \$300 million annual price tag.

It's also worth noting that FirstEnergy announced that *all* of its nuclear units cleared in the most recent PJM Base Residual Auction obligating them to deliver power in 2020-2021 delivery year. Under PJM's Capacity Performance rules, that means those units, or their equivalent, are required to deliver power *into the next decade*, preserving those jobs until *at least* then. And, while it is true that those plants could still retire before then, FirstEnergy would have to somehow replace those obligations *at a significant cost*. (More on the recent PJM capacity auction to follow).

Price Stability

Utility bills in Ohio are already stable; power prices are and have been falling for years. In Chuck Jones's testimony he noted Ohio's power prices before re-structuring were 22nd in the country and today are 22nd in the country. Although wholesale power prices are down significantly, new charges in the form of riders have kept consumer overall utility bills flat. Ohio consumers haven't benefited as fully as they should from restructuring because companies like FirstEnergy and AEP continue to add fees to consumers' bills via riders that ensure they collect stable revenues regardless of power prices.

Additionally, if this bill is enacted it ensures higher costs to consumers for the next 16 years – it provides price stability but at guaranteed higher prices and only FirstEnergy benefits. FirstEnergy and other witnesses have pointed your attention to

a Brattle report that suggests if the uneconomic, high cost nuclear units are retired and replaced by lower cost, higher efficiency natural gas units consumers will pay \$177 million more for electricity. Only an economist supporting FirstEnergy's position could produce a report that says replacing higher cost power with lower cost power will result in higher charges to consumers. A proper study of this question would determine if the supply curve shifted but more importantly what would be the impact on the clearing price before assuming that higher costs are a certainty.

Customers in Ohio that shop for their electric supply in the retail market can already secure price certainty in the market by selecting a fixed rate option in their supply agreement. There are contracts already available to residential customers of various terms that ensure their price remains fixed and stable. Commercial and industrial customers can also secure fixed prices and use any number of hedging, demand response and other tools to ensure their prices remain stable and predictable. I should also note, customers can secure green energy or zero emission products today, without out-of-market payments. This program destroys those benefits by making shopping customers pay this unnecessary charge as well. To say it doesn't impact customers' ability to shop the competitive retail market because everyone is required to pay is the same as saying that an increase on food and beverage taxes does not impact a consumer's ability to shop because they can still shop at whatever grocery store they choose.

Finally, as mentioned above, FirstEnergy recently announced that it cleared all of its nuclear generation in the most recent capacity auction. This means that FirstEnergy must have offered those plants in at zero dollars, or some cost below the clearing price. Each generator decides its own bidding strategy in the PJM capacity auction, and it's completely irrational to offer plants that FirstEnergy has stated have a high operating cost at below-market prices, and worse yet, for FirstEnergy to then complain that the market is broken. This is like a gas station that sells gas for less than their cost and complains when it loses money that prices aren't high enough to remain open.

This strategy negatively impacts the overall PJM capacity market and the capacity revenues received by generators. While some companies elect to be price takers and bid in at zero (or less than their costs), it is typically generators that have sold their capacity prior to the auction or are receiving cost recovery via rate-based treatment. The fact is that a plant, particularly one that is losing money, should be bid in at its actual costs to ensure that the market can send the appropriate price signals for investment and retirements and the capacity price reflects the actual cost to provide service. It's disingenuous to offer your product at below-market prices and then complain that the market is broken.

Economic Development

Dynegy, like virtually every other power producer, would like to see steady growth in every state's economic development. After all, our employees live here as well and economic development means more customers and more opportunities for us to compete and deliver power to customers. But one of the basic tenets of sound economic development is the need for low cost power.

How will northern Ohio businesses in particular, but all of Ohio if other possible re-regulation ideas are introduced, remain competitive when shouldering the burden of increased costs to the tune of \$300 million or more for ZENs, on top of the additional \$200 million for the next 3-5 years for the Distribution Modernization Rider that the PUCO has already awarded FirstEnergy? A rate increase of \$500 million is crippling to economic development opportunities and creates long-term problems for existing businesses that have to look at ways to minimize their costs.

In addition to being disadvantageous to northern Ohio, it makes Ohio overall less attractive for companies who are looking to locate or expand their operations here. Energy is a critical element to securing economic development opportunities. Ensuring the availability of lowest cost power solutions and fostering the competitive retail energy market are key attributes of a vibrant and healthy business environment; burdening businesses with unnecessary subsidies lessens Ohio's ability to retain and attract employers.

"Home Grown" and "Base load" Power

Ohio has historically been an importer of power, and there's a simple reason for that: States that are part of a regional grid benefit from obtaining electricity at the lowest cost and greatest reliability. It's the basic reason why Ohio is part of PJM. Also, because of its strong manufacturing-based economy, Ohio has imported power at some level for decades. It is important to note that in 2011, Ohio imported less electricity than it did under the vertically integrated model. The reason is that the competitive markets drove investment.

Ohio's generation fleet is undergoing a significant transformation due to the development of local shale resources. Power plant developers want to locate in Ohio to take advantage of low cost fuel and the ability to access the PJM market, where the most economic and reliable units are rewarded for their performance. If the markets are allowed to work, and Ohio can leverage its access to low-cost natural gas, it's not hard to envision that Ohio could quickly become a net exporter in the near future.

Importantly, Dynegy is not coming to the Ohio General Assembly seeking support or subsidies. As a competitive generator it is incumbent on our team of employees to perform at the highest level and operate our facilities in the most safe, reliable and efficient manner. For example, we have invested more than \$50 million into the Zimmer facility in southwest Ohio and as a result of our improved operations have reduced the outage rate from nearly 30% to less than 10%. By making that investment, we are doing what is necessary to ensure the greatest opportunity for success in the market. Being forced to compete against subsidies and generation that can afford to be agnostic about operational costs leaves generators like Dynegy fighting an uphill battle and puts the investments we have made in Ohio at risk. If the general assembly is going to eliminate competition by picking winners and losers through subsidies to those who can't compete, unsubsidized generation will likely retire and prices will increase.

Imports fluctuate and Ohio should be most concerned about securing reliable, low cost power regardless of where it comes from. Ohio could commit to generating more than 100% of its power from in-state resources and becoming an exporter to neighboring states but there is a cost associated with doing so. FirstEnergy rightly pointed out in 2011 that even under vertically integrated model power plants that used to be regulated weren't always built in Ohio because new siting decisions are based on many factors including water, space, and fuel source resulted in them being located in other jurisdictions.

There is nothing in Ohio law that prevents any Ohio based utility from constructing a new power plant via their unregulated generation affiliate. They simply choose not to do so. Instead they are asking you to ensure they continue to collect revenue for plants that are no longer economic.

There is also much rhetoric around "saving base load power plants." What's important to note is that "base load" isn't a reliability attribute; it's a measure of a plant's ability to operate at full output for extended periods of time. While coal and nuclear plants have traditionally been thought of as "base load" plants, many natural gas plants are now base loaded because of their price advantage. And, natural gas plants are the best kind of base load there is: In addition to running flat-out, they can ramp up and down quickly, something nuclear plants can't do.

Grid Reliability and Resiliency

In addition to the arguments around "base load" power, the fact is that many power plants have attributes that contribute to power grid reliability and resiliency. For example, nuclear plants do not cycle or ramp up and down like natural gas fueled units; nuclear plants are either on or off, and do not respond well to ramping up and

down to follow changing customer usage. This makes them the least effective form of generation to partner with the evolving electric grid where greater renewables and their intermittency challenges are the current reality. Also, during grid disturbances, nuclear power plants are some of the first plants to trip offline, as to protect the nuclear reactor against a nuclear meltdown and radiation emissions; and, those plants cannot start without offsite power or the benefit of other more flexible plants. These not-so helpful “attributes” of nuclear plants hardly contribute to grid resiliency or reliability.

ZEN credits are not RECs

It is critical to note that ZENs are **NOT** the same as RECs, or renewable energy credits. Renewable energy credits operate in a market construct where supply and demand dictate the value of the RECs and all qualifying resources can compete.

The ZEN program is applicable only to nuclear units owned by FirstEnergy and the value of the ZENs are set in statute with an adjustment mechanism that almost guarantees costs continue to increase. While the bill seeks to minimize the impact by limiting the increase to customers to no more than five percent (5%), it also provides a mechanism to create a deferral for any charges above the five percent increase. And, while some argue that only a 5% increase per month to a residential customer is a small price to pay, what about the struggling business owner who will be paying thousands for this subsidy, or the large manufacturer who will be paying millions? And, the deferral hides the actual cost of the subsidy and creates another cost (likely yet another rider) that customers will have to pay, with interest creating a revenue stream for FirstEnergy or any subsequent purchaser of the assets.

What is the Alternative?

Substantial investment in Ohio is happening in a variety of ways. First, companies like Dynegy have invested billions of dollars to acquire existing generation assets from utilities that no longer wanted to operate in a competitive market. Dynegy made the decision to buy assets in Ohio because we believe they can be operated profitably, and it's at our risk if we can't succeed in doing so. If we can do so, our investors and shareholders benefit - just like the utility's shareholders benefit from their profitable operation. I'm told former Governor James Rhodes once said, “Profit isn't a dirty word in Ohio.” We agree. The question is, is there an opportunity for all power producers to earn a profit in Ohio or will profits only be guaranteed to certain companies in statute, to the detriment of those companies that rely on competitive markets?

It is noteworthy that there are approximately 10,000 MWs of new, clean, lower emitting natural gas fueled plants that developers are bringing to Ohio. These new plants are choosing Ohio because of low cost fuel and a seemingly well-functioning market that rewards low cost generation. The 12 power plants that are under construction, have Ohio Power Siting Board approval, or are in application or development phase are located mainly in eastern Ohio.

Responses to Prior Testimony

You have heard testimony from a number of parties either supportive of or interested in the bill before you. I would like to take a moment and respond to some of the claims that have been made and give you a different perspective to consider.

One is that markets don't value zero emitters. The fact is that the markets don't value clean, low carbon, efficient, fast-ramping natural gas plants, either. So, given that a number of states outside Ohio have interest in building carbon pricing into the PJM market, PJM is undertaking a process to allow states to just that. Like electrons, Carbon molecules don't recognize state lines and if this issue is going to be addressed, a regional or national approach is the right way to address it.

It is clear that the Polar Vortex of January 2014 has become the poster child for why nuclear subsidies are warranted. I disagree. Attached to my testimony are some facts from PJM reports concerning the outages that occurred during January 2014. You will note that outages happened across ALL fuel sources, including nuclear, coal, natural gas, and renewables.

The implication being made seems to be that natural gas resources are unreliable in times of high system demand and only nuclear and coal plants can remedy that weakness in the system. I think you need to look at actual experience and lessons were learned by plant operators and the grid operator, PJM. The lessons learned include the following:

1. *All* sources of generation have the potential for unforced outages regardless of fuel source;
2. The market will respond to those challenges (*e.g.* Capacity Performance requirements established by PJM) and achieve better outcomes (even FirstEnergy has stated that PJM has not triggered a shortage event since implementation of its Capacity Performance product); and
3. Natural gas generators that previously may have operated without firm gas supply now must secure firm supply to ensure their ability to run when called.

Note that the market evolved in response to the polar vortex event to implement new and improved requirements that will apply to all generators, including Dynegy, and customers are better served as a result.

Lastly, testimony has been provided to this committee that the competitive generators oppose the subsidies in IL and NY because we want prices to rise and to profit from those closures. Before getting to that question, let's look at who will benefit from the bailouts and how much. In New York, one company is slated to receive \$8 billion. In Illinois, the cost of the bailouts will be \$3 billion. All of those costs are being awarded to *one company*. If power prices were to rise due to plant closures, the market would respond to mitigate those increases by signaling for new, lower cost generation to be built. Much like with this ZEN proposal, in New York and Illinois the winner of the subsidy wants to keep all of the money and prevent others from participating in a well-functioning market. To me, that doesn't sound like a market, but the result of a state picking winners and losers.

Conclusion

A number of witnesses, including FirstEnergy CEO Chuck Jones, have referenced the following testimony offered in October 2011 concerning competitive markets. It is as true now as when it was offered.

“First, with respect to electric generation, competitive markets work. They deliver the lowest price over the long term to customers, and the proof is undeniable.

Second, measures that restrict customer shopping or subsidize one electric generator over another are throwbacks to monopoly regulation. Such efforts that pick “winners” and “losers” in the energy market would create obstacles to private investment in generation and increase prices for customers.

...more important, all of [FirstEnergy's] generation-related investments – including the risks that accompany them – are now borne by [FirstEnergy] shareholders and not by customers.”

I completely agree with those statements. Those assertions, dare I say facts, remain true regardless of a specific company's financial performance over time. The only change is the economic condition of the company seeking to reverse course and avoid the outcomes being dictated by the market.

Over time we learn that facts, circumstances, and assumptions can and do change. In 1999 power prices were high, demand was growing, and customers wanted to secure

lower cost power from the market. In 2008, before the economic meltdown basic assumptions about load growth (it would increase) and high gas prices (that prices would be high for the foreseeable future) caused policymakers to adjust the law presumably in an effort to protect customers from ever increasing costs.

In an industry as large and complex as the electricity industry policy makers should set a course and pursue it to its logical conclusion, not ignoring bumps in the road or changing conditions, but responding to them while advancing toward the ultimate outcome.

When customers save money, where investment in new and existing competitive generation is happening, and where the power grid remains reliable, there is no rational basis for reversing course and returning Ohio to a regulatory paradigm that looks more like the 1960's than the 21st century.

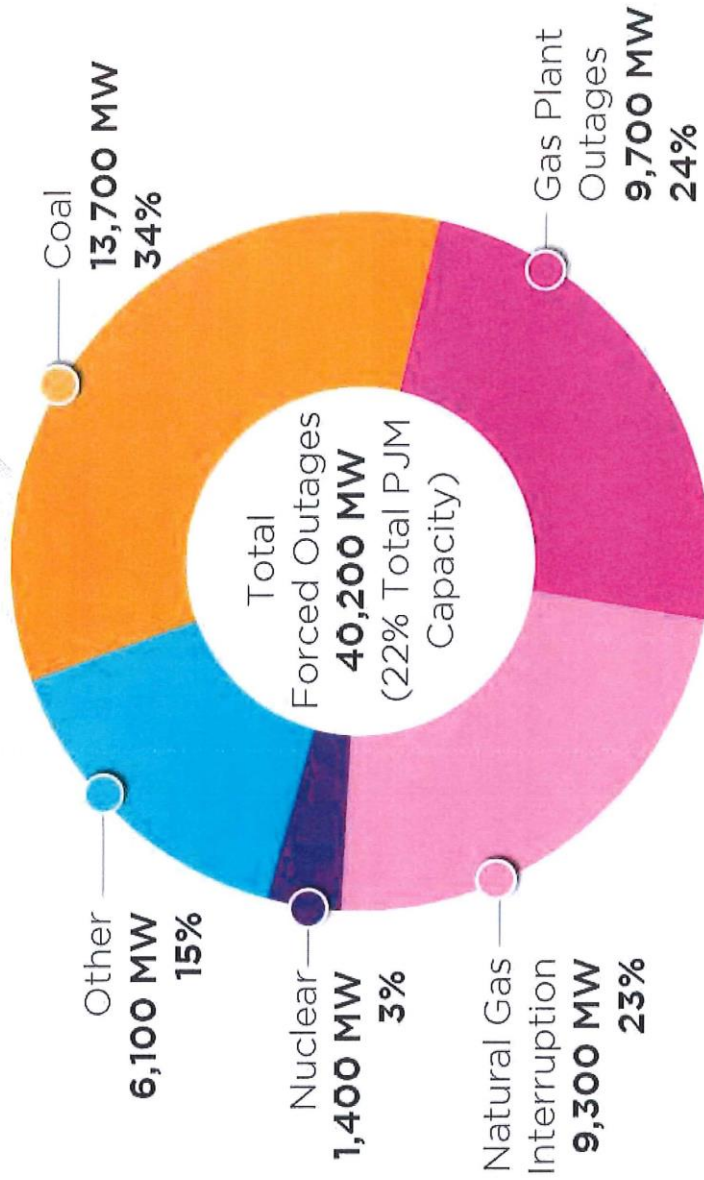
Thank you for the opportunity to testify today. I am happy to answer any questions.

Exhibit 1

Polar Vortex Outages



Forced Outages – January 7 Evening Peak (7pm)



Detailed Outage Causes

