

HOUSE RESPONSES TO EACH CLAIM MADE BY THE OHIO COALITION FOR AFFORDABLE POWER ON APRIL 10, 2008 ABOUT SB 221 AS INTRODUCED IN THE HOUSE PUBLIC UTILITIES COMMITTEE

Coalition Claim:

This bill is worse for consumers than S.B. 3. Taken as a whole, this bill could lead to circumstances where Ohio rate payers will be paying rates higher than market rates. When multiple surcharges are layered on top of rates which could start at levels close to market, Ohio consumers could be put in the worst of all worlds.

House Response:

The House Bill was specifically designed to assure that customers never pay more than the market option. Substitute SB 221 provides that an ESP, including all of its terms and conditions (for example any escalators) must be more favorable than the market option before the PUCO can approve the plan. This is the same type of analysis that the PUCO has used in approving rate stabilization plans (RSP's) that have served customers well over the last several years.

- Electric Security Plans (ESP)

Coalition Claim:

No ESP Price Protection

The standard for judging the reasonableness of an ESP seems vague, particularly as compared to the description in the House's "Energy for Ohio's Future" summary on page 6, which states that the ESP must be "lower than the market rate offer and overall more favorable for consumers." The standard in the bill is "favorable in the aggregate as compared to the expected results that would otherwise apply." (lines. 1064-1066) This ambiguity would allow the Commission to approve an ESP at virtually any rate.

House Response:

The House Bill mandates that the PUCO can only approve an ESP if the PUCO determines that it is, in the aggregate, "more favorable" (line 1064) to consumers.

Coalition Claim:

No Objective Criteria for Rates

Overall, the bill fails to tie utility rates to costs, “just and reasonableness,” earnings of the utility, or any other measurable standard, except where the concept of “cost” benefits utility (e.g., 4909.143, establishing the ESP only ties rates to costs when it deals with automatic cost increases for the utility). This sets up a process whereby rates will be litigated at the PUCO where utilities have considerable advantages over consumers.

House Response:

The bottom line established by the House Bill is that the ESP result approved by the PUCO must be “more favorable” to consumers than the alternative. The House Bill (unlike the Senate version) requires all utilities to file an ESP.

The House Bill, unlike SB 221, does not lock utilities’ significant stranded costs into future rates.

Unlike SB 221, the House Bill does not perpetuate subsidies for “special contract” customers.

The process specified in the House Bill requires notice, an opportunity to be heard and a hearing. This is the same process that has been used at the PUCO for many decades.

On one hand, the House Bill is being criticized because it does “not provide sufficient incentives to ensure a reliable supply of electricity.” On the other hand, the House is being criticized for not limiting electric rates to the historic costs that do not include the costs that must be incurred to meet reliability objectives. The House Bill strikes a balance between pricing and reliability objectives.

Regarding the reference to 4928.143 (incorrectly cited as 4909.143), such cost increases would have been greater under cost-based ratemaking because they are only part of the cost of providing service.

Coalition Claim:

No Rate Recognition of Plant Retirements or Sales

The bill will allow a utility to retire or sell a major generation asset without any corresponding requirement to reduce rates to reflect that retirement or sale.

House Response:

The House has an amendment to address this issue. The amendment will give the PUCO the discretion and authority to consider plant retirements as part of the ESP process.

Coalition Claim:

Cost Concepts Apply Only to Expensive New Generating Assets

There is an unfair asymmetry in allowing the automatic recovery of the costs of expensive (above market) generating units (e.g., Ins. 973-1009) without any recognition of the true cost of existing generating units (below market), including cost reductions from depreciation and retirements.

House Response:

There is no opportunity for an above market outcome in the House Bill.

There is no provision for automatic recovery of costs associated with “above market generating plants” in the House Bill. Before any new plant cost is recoverable by any utility under an ESP, the PUCO must first determine that the plant is needed (see line 1003) to meet reliable service to customers and the need must be satisfied through the discipline of a competitive bidding process (see line 996).

Under cost-based ratemaking, which is what is described above, utilities were monopolies that had captive customers with no choices. The House Bill recognizes that competition and customer choice will provide customers with the best price, innovation, and efficiencies and therefore preserves that option for customers.

Coalition Claim:

Absolute Utility ESP Veto Power

The bill at lines 1073 to 1086 gives the utility an absolute veto over any changes made by the PUCO to an ESP as filed, allowing the utility to go to the MRO whenever the PUCO modifies the utility’s desired ESP. This invests the utility with enormous bargaining power.

House Response:

Under current law and as mandated by SB 3 and confirmed by PUCO decisions, a utility has the right to go to market. The House Bill requires a utility to file an ESP. If an ESP cannot be agreed upon, the utility may file

an application for an MRO which must meet numerous criteria to be approved by the PUCO. For any utility that continues to own generation that was “used and useful”, the path to a market-based rate proceeds on a gradual course that involves blending prices in ways that give the PUCO the ability to avoid “rate shock”.

Coalition Claim:

No Due Process or Transparency in Approval Process

Nothing in the bill requires the Commission to hold public hearings or rate cases before approving multi-billion dollar plant additions or plant retirements. This violates SB 221’s original desire for openness and fairness in utility rate-making.

House Response:

The only time the House Bill allows the PUCO to consider and address the cost of new generation plant is in the context of an ESP and the House Bill requires notice, an opportunity to be heard and a hearing for all ESP proceedings (see Section 4298.141, starting at line 761). The PUCO cannot allow new plant costs unless it determines that it is needed and then the need must be met through a competitive bidding process. As noted previously, the House has an amendment to address retirements.

Coalition Claim:

Utilities May Escape from PUCO Jurisdiction

The bill at lines 1228 to 1233 allows a utility to sell their generating assets after January 1, 2013 or the end of its first, approved market rate offer under section 4928.142”, whichever is later, without Commission approval. With such a sale, the Commission can lose all jurisdiction to regulate its generation rates (as claimed by FirstEnergy).

House Response:

The House Bill does not permit a utility to transfer or sell generating assets until it has completed the full transition to the market under the regulation and oversight of the PUCO. The House Bill makes it clear that the MRO must run its complete course, as determined by the PUCO. In no event can the PUCO permit a transfer prior to 2013.

SB 3 gave utilities the unilateral right to transfer or sell generating plants without PUCO approval. In fact, SB 3 encouraged utilities to do so and the PUCO has already approved some transfers that cannot be undone. The

House Bill takes away this right going forward as part of its rate stability and predictability provisions. It gives back this right once the PUCO-controlled transition to market is complete. Any new generating plants built as part of an ESP must be dedicated to serve Ohio's citizens for the life of the facilities. No generating plants can be sold without PUCO approval if it is subject to a non-bypassable surcharge.

Coalition Claim:

Rate Shock of 80% - 90% Will Occur for Ohio Power's Customers

The failure of Sub. S.B. 221 to base ESP generation increases on any consideration of the cost of the legacy generation or the earnings of the utility would cause the generation rates of Ohio Power's customers to increase by at least 80% - 90% in no longer than 5 years. This 80%-90% rate increase will be compounded by:

1. The non-bypassable cost of above market new clean coal generation (lines 973-992)
2. Mandated very costly renewable resources with no price caps (line 1566-1588), and
3. for distribution services "single issue ratemaking", a "revenue decoupling mechanism or any other incentive ratemaking", "modernization incentives", and recovery of "lost revenue." (lines 1038-1049).

All told, Sub. S.B. 221 would cause the rates of Ohio Power to go from about the lowest in the United States to the highest. The economic effect from this massive transfer of wealth from Ohio rate payers, of approximately \$800,000,000 per year by the end of year five, to Ohio Power's shareholders would be significant.

House Response:

All the stakeholders, their lawyers and experts have acknowledged during the House and Senate hearings that electric prices are going to increase. There is no market-based or cost-based system that can defy fundamental forces. This is not the result of a choice between markets or regulation. It is the result of the larger forces at work on our economy whether you are a manufacturer of electricity or steel.

It is difficult to deal with claims about future rate increases without seeing the basis for the claim. Nonetheless, the current environment means that Ohio Power's costs will increase. The House Bill gives the PUCO clear

authority to ensure that any increase in Ohio Power's rates occur without causing abrupt (see line 928) increases when prices are set under the MRO. Under the ESP, the PUCO has the same opportunity by using its phase-in authority. What ultimately happens is up to the PUCO.

The House Bill makes sure no new generation comes in above the market price because it must be procured through a competitive bidding process. The Senate version of the Bill has no such protection.

The House has heard its Senate partners and the Governor regarding their desire for a price cap for renewables and the House and is willing to discuss.

The Bill passed by the Senate (beginning at line 1831) required a utility with an ESP to file an infrastructure modernization plan and treated this subject as a stand alone (single issue) opportunity to adjust rates. Thus, the Bill passed by the Senate provided for single issue ratemaking. In the House Bill, the treatment of infrastructure modernization cost is not singled out; it is considered as part of an ESP package, which can only be approved if the package is better for customers.

Coalition Claim:

Encouragement of a Monopoly

The bill at lines 1011 to 1017 allow a utility to implement ESPs that include "[t]erms, conditions or charges relating to limitations on customer shopping for retail electric generation service, by passability ..." and numerous other provisions which attempt to restrict consumer choice and could result in a deregulated monopoly.

House Response:

The House bill requires utilities to propose an ESP, and the commission may only approve the ESP if it is more favorable to consumers than the alternative, resulting in the utility receiving less than market prices. Accepting a price that is lower than it could otherwise obtain only makes sense if the overall package, including the lower price, is reasonable for both customers and utilities. This historical risk/reward trade off, which involves using provisions like those cited above, has benefited consumers through RSP's in the past. Such concepts are designed to lower costs to customers and would be implemented only upon commission approval.

Coalition Claim:

Special Contracts

The bill at lines 524-526 prohibits virtually all Commission-approved special contracts, gravely limiting the State's ability to compete for new businesses and retain existing businesses.

House Response:

The House has indicated to its Senate partners that it has been and remains willing to address this issue.

Coalition Claim:

Side Deals

The bill fails to prohibit secret side-deals.

House Response:

Neither the bill submitted by the Governor nor the Bill passed by the Senate prohibited side deals. They addressed the ability to discover side deals in PUCO proceedings. Because an Ohio Supreme Court decision addressed this exact issue and mandated that parties have discovery rights in the case of side deals, the House did not feel the subject warranted specific statutory treatment to accomplish the transparency objective. To make it abundantly clear that the House supports the transparency objective served by the Senate Bill, the House has an amendment to address transparency objectives.

If the Governor and the Senate wish to ban side deals, current and prospective side deals, the House stands ready to amend its bill to do so.

Coalition Claim:

Special Benefits for FirstEnergy Under an ESP

The bill at lines 967 to 972 allows a utility, through an ESP, to automatically recover from retail customers "purchased power acquired from an affiliate." The FirstEnergy companies will be able to recover the wholesale market price of all of the power they sell to retail customers while at the same time realizing all of the benefits to utilities that have elected the ESP, e.g., non-bypassable new power plant surcharge, automatic increase of ESP components, limitations on shopping, and single-issue ratemaking for distribution rates. This will almost assuredly result in rates that are higher than market.

House Response:

The House Bill mandates, first and foremost, that any ESP, including all its terms and conditions, be more favorable than the market option (see lines 1060 to 1066 and 1109 to 1116). Therefore, the situation described above CANNOT HAPPEN!

The Bill passed by the Senate (beginning at line 2035) authorized the PUCO to approve automatic increases in rates. It also provided for recovery of purchased power costs (see lines 2008 and 2009).

As confirmed by the hearings before the House, FirstEnergy's opportunity to recover its wholesale purchased power costs is related to the requirements of federal law and the U.S. Constitution.

The House Bill will not permit FirstEnergy or any other utility to extract ESP benefits from one provision while avoiding responsibilities under other provisions. The House Bill instructs the PUCO to evaluate the effect of the ESP based on its provisions in the aggregate. The ESP must be better than the alternative before it can be approved by the PUCO.

Coalition Claim:

Strategic "Gaming" of Power Plant Construction

The bill, beginning at line 1005, appears to allow a utility that is recovering the cost of a new power plant through a non-bypassable surcharge to withdraw the plant from dedication to Ohio consumers simply by forgoing the surcharge. This would allow the utility to strategically sell the plant's output on the market once it has been depreciated to a point where market sales would be economically beneficial to the utility.

House Response:

The House Bill, which contains the text beginning at line 1005 referenced above, is clearly intended to dedicate the output of new generation to Ohio's consumers for the life of the facility if the utility obtains PUCO approval of a non-bypassable surcharge. The House Bill (beginning at line 1066) also requires the PUCO to make sure that the benefits derived from a surcharge are made available to those who bear the surcharge. Lastly, the PUCO must approve the transfer or sale of any generating plant that is subject to a non-bypassable charge (see lines 1237 – 1240) under all circumstances.

The House will consider suggestions to make sure this intent is beyond question.

- Market Rate Option

Coalition Claim:

MRO Exit Ramp is Illusory

The qualifying criteria for MRO option (at Ins. 809-826) are not true gauges of the existence of a competitive retail market. All could be instantly met by all Ohio utilities, notwithstanding the fact that there is no competition for retail electric service in Ohio by any meaningful measurement.

House Response:

The market criteria (set forth in lines 809-826) are legitimate standards to be met in order to test for a competitive market for electricity. Membership in an RTO means nondiscriminatory access to transmission for all market participants. A market monitor assures proper market behavior and the availability of pricing information out in the future at least two years allows market participants and customers to plan.

But even if the PUCO finds that the criteria has been met, the House Bill gives the PUCO the authority to ensure that the end result is not abrupt increases in rates.

The dynamic between the utility's SSO price and market price will always be present as prices vary through time, and is not an indication of a flaw in the market criteria contained in SB 221 or the lack of a robust retail market for electricity.

- Renewable Power and Energy Efficiency Provisions

Coalition Claim:

Renewable Power Provisions – No Consumer Protections

The bill does not contain cost-caps on alternative energy resources. The utilities are required to meet the annual targets. Because the bill requires that penalties for not meeting the annual targets be levied on the utility and not be passed-through to consumers, the utility has a strong motivation to meet the targets irrespective of the cost to consumers.

House Response:

The House has heard its Senate partners and the Governor regarding their desire for a price cap for renewables and the House is willing to discuss.

Coalition Claim:

Renewable Power Provisions – Unreasonable Timelines

The bill mandates renewable energy standards at the end of 2009. Indications are there is a backlog of available manufacturing capacity for these sources of generation, in addition to reasonable contracting, siting, and other logistical aspects of bringing renewable energy resources to Ohio. The start of any mandate should begin no earlier than 2015, to allow reasonable least-cost planning and rational implementation of those plans.

House Response:

The House disagrees based on what experts and industry representatives have repeatedly stated in testimony.

Coalition Claim:

Demand Side Provisions – No Cost-Benefit Justification

The bill, beginning at lines 1691, sets energy efficiency targets for utilities without requirement of a cost-benefit analysis of the measures that a utility might undertake. This could result in a circumstance where the cost of such reductions in demand is greater than the cost of incremental generation, whatever its source. Additionally, the rate payers shoulder this risk because the utility is assured recovery of its demand side programs. Demand side benefits which should be applied to the “demand side” are transferred to the supply-side, e.g., the utilities.

House Response:

The Senate Bill includes specific policy goals directed at encouraging demand side management. The House Bill builds on the Senate Bill’s policy by bringing customer-sited demand side management into the portfolio mandates included in the House Bill in ways that should be substantially useful to Ohio’s business customers.

Coalition Claim:

Immeasurable Demand Side Provisions

As a general matter, the bill’s efficiency provisions lack clear measures. It is unclear whether baseline demand can be meaningfully measured against the sources of future changes in demand.

House Response:

The House Bill (such as at lines 1744 through 1748) provides for such adjustments as may be appropriate to address future changes in demand.