Before the Ohio House Public Utilities Committee

Prepared Testimony of

Jonathan A. Lesser, PhD

President, Continental Economics, Inc.

February 19, 2014

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Good afternoon. My name is Jonathan Lesser. I am the President of Continental Economics, Inc., an economic consulting firm specializing in economic and regulatory matters affecting the energy industry.

Last October, I testified before the Committee and addressed the theory of wholesale market “price suppression” that opponents of any proposed mandate reforms have relied on during their campaign to maintain the current annually escalating electricity usage reduction mandate. The mandate’s usage reduction requirements are set forth in R.C. Section 4928.66.

Prior to and after my testimony in October, we attempted to obtain the details behind the “studies” which the reform opponents have referenced from time to time so that we could test the quality, inputs, assumptions and predictive value of the models which are only generally described in the materials distributed by the reform opponents. However, these critically important details were not supplied. So, I was asked to evaluate the price suppression claim based on observable data and prepare a report on my findings.

The purpose of my testimony today is to provide you with a brief overview of my findings regarding reform opponents’ wholesale price suppression claims as well as the related claim that this theorized wholesale electric price suppression is benefiting Ohio's electricity consumers by an amount in excess of the cost these consumers pay as a result of the usage reduction mandate.

The report that is provided with my testimony was prepared at the request of the Industrial Energy Users-Ohio ("IEU-Ohio") which I understand to be part of a broader informal association of businesses, business organizations, and labor organizations, called "Ohioans for Sustainable Jobs."[1]

For purposes of my analysis and report, I focused on the most frequently referenced "study" which the reform opponents attribute to the Advanced Energy Economy Ohio Institute ("AEEOI"). A high-level summary of the results of that study was released on September 25, 2013, although the full analysis and assumptions used in that report have never been provided. My understanding is that this summary has been relied on by opponents of H.B. 302 to support their position that the annually escalating electric usage reduction mandate must be left as-is, regardless of the changes in circumstances since the mandate was enacted. The AEEOI study asserts that by mandating reductions in the electricity usage of Ohio's retail electricity users, or at least the retail customers served by electric distribution utilities ("EDUs"), wholesale electric prices are "suppressed" and that

[1] It is my understanding that Sam Randazzo has previously testified before this Committee, and has provided you with information about the membership of IEU-Ohio and its positions regarding proposals to reform Ohio's supply side and demand side portfolio mandates. Accordingly, I will not describe IEU-Ohio as part of my testimony.

this wholesale price suppression results in equally lower Ohio retail electric prices. Thus, the hundreds of millions of dollars Ohio's retail electricity consumers are paying each year as a result of the electricity usage reduction mandate are, according to this price suppression benefit theory, providing Ohio consumer benefits in excess of the significant costs incurred by Ohio's consumers to produce the wholesale price suppression result.

I will begin my testimony with a brief overview of the electricity usage reduction mandate and then explain the results of my efforts to test the reform opponents' claim that their theorized wholesale price suppression is providing Ohio customers with a retail price benefit in excess of the retail charges they are paying due to the mandate.

Although the mandate is often referred to as an energy efficiency mandate, it is more accurate to describe it as an arbitrary directive that each year forces ever higher reductions in the electricity usage of Ohioans. The amount of the forced reduction in usage is unrelated to the actual efficiency of customers' pre-existing electric usage.

The mandate is uniquely applied to EDUs and their customers; it does not apply to Ohio municipal utilities or electric cooperatives, which together supply about ten percent of Ohio's retail electricity demand.

Since 2009 and through the end of 2014, Ohio's EDUs will have spent, at consumers' expense, over $1 billion to comply with this mandate.

Because Ohio law requires the EDUs to reduce consumers' electricity usage by ever increasing amounts (totaling at least 22% by the year 2025), and because forcing the higher future usage reductions will be more costly to achieve as less "low hanging fruit" remains, the cost of complying with the mandate will certainly continue to increase as it has since the mandate's inception. Since 2011, the EDUs' mandate compliance budgets have grown at an average rate of 12% per year. If that rate of growth continues, by 2020, *Ohio electric consumers will be paying over $500 million per year as a result of the Ohio electricity usage reduction mandate*.

Those who argue in favor of retaining the current electricity usage reduction mandate have asserted that Ohio's retail electric consumers will receive a "free lunch." This "free lunch" assertion rests on their layered claim that: (1) the mandate suppresses the *wholesale* electric price in a multi-state region; (2) the amount of this suppression flows directly into the *retail* electric prices paid by Ohio's retail electric customers; and (3) the effect of the *retail* price reduction produces a direct Ohio retail consumer benefit in excess of the cost of the mandate tax paid by these same retail consumers. As you may recall from the testimony that I understand has been presented to the Committee, Ohio is part of the PJM Interconnection, LLC ("PJM") regional transmission organization. Ohio is not an electrical island.

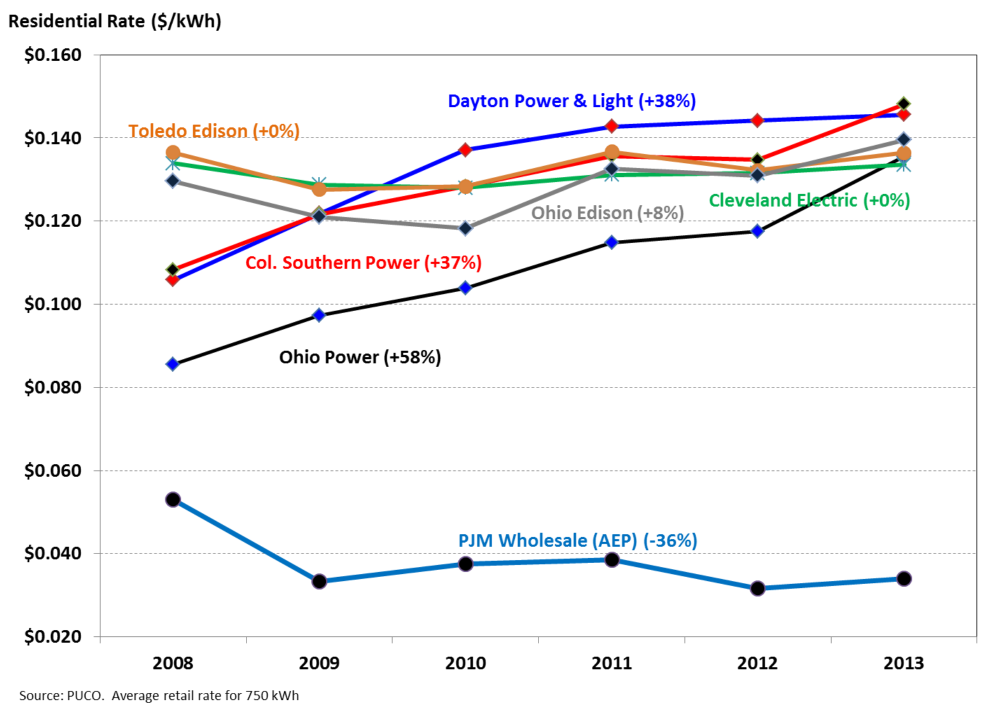
PJM has a footprint that covers all or parts of 13 states and Washington, DC. In addition to coordinating all of the electric generating plants in the region and ensuring the power system operates safely and reliably, PJM oversees a wholesale energy market in which bids and offers from buyers and sellers set market-based wholesale prices for electricity every hour.

Because the PJM wholesale market is integrated throughout this region, the effects of any forced electricity usage reduction in Ohio as a result of the mandate are spread throughout the PJM region. As a result, 80% of any wholesale suppression "benefits," if they even exist, flow to customers outside Ohio and customers of Ohio municipal utilities and cooperatives, which are exempt from the usage reduction mandate and the mandate tax. Thus, 80% of the alleged benefits accrue to "free riders" who do not pay for those benefits.

Using data for 2012, my analysis shows that the typical Ohio residential customer using 750 kilowatt-hours ("kWh") of electricity each month received, *at best*, a 37 cent reduction in their monthly electric bill. I say "*at best*" because, as I describe in more detail in the full report that is being submitted with my testimony, the simplifying assumptions I made for the purpose of testing the reform opponents' claims err on the side of maximizing the amount of alleged wholesale price suppression that might be available to retail electric customers of Ohio's EDUs.

At worst and, in my opinion, far more likely, there is no wholesale price suppression benefit to offset the real, known and measurable cost of the mandate, which is being paid by the retail electric customers of Ohio's EDUs. ***To obtain the wholesale price suppression benefit theorized by the reform opponents, those same Ohio residential customers pay a monthly mandate tax ranging between $1.74 and $3.92, or between five and ten times greater than the theorized price suppression benefit. In other words, Ohio's retail electric consumers are paying between $5 and $10 for every $1 of retail price suppression benefit that the reform opponents' wholesale price suppression theory might allow and as it may relate to the customers paying the mandate tax.***

Moreover, Ohio's retail electric prices have not decreased or tracked wholesale electric prices, as the reform opponents claim. Between 2008 and 2013, average wholesale electric prices in PJM decreased by over one-third. Yet, retail electric rates charged by Ohio's EDUs have increased as much as 58%. The increases in retail electric prices in Ohio are not solely due to the electricity usage reduction mandate tax. As I explain in my report, there other contributing factors. But as the chart below indicates, there is no direct or necessary relationship between the observable trend in wholesale electric prices in the PJM market and the trend established by observable retail electricity prices paid by Ohio consumers.



My analysis of the observable data leads me to three conclusions:

1. ***If the reform opponents' wholesale price suppression claim is correct, then the biggest winners from the Ohio electricity usage reduction mandate are the consumers and market participants inside and outside Ohio who do not pay the mandate tax***. To the extent that the Ohio mandate really has "suppressed" PJM wholesale electric prices, the in-state and out-of-state consumers and market participants who do *not* pay the mandate tax are

collectively capturing 80% of the suppression benefit theorized by the reform opponents. These consumers and market participants are classic "free-riders."

2. ***Ohio businesses are therefore being forced to subsidize some of their out-of-state competitors, including those competitors within the PJM region that are not subject to any mandates or their costs.*** Thus, the reform opponents are implicitly urging Ohio's leaders to leave in place a law that gives out-of-state businesses a competitive advantage while imposing a competitive disadvantage on in-state businesses. Doing this cannot possibly enhance economic growth, job retention and job creation in Ohio.

3. Ohio consumers and businesses are suffering economic harm *because* of the mandate. The reform opponents' claim that Ohio retail electric consumers will be harmed if the current mandate is reformed is unsupported by the wholesale price suppression theory they advance, and in conflict with the rising Ohio electric bills that Ohio retail electric customers are paying in the real world.

Thank you for this opportunity to testify before you today. I look forward to answering your questions.