

Ohio's Electric Restructuring Gap
Legislation Is Needed Now to Mind the Gap and Advance Ohio's Policy Objectives

Objective 1: Provide the PUCO with the Obligation and Clear Authority to Establish Default Generation Supply Prices Until There is Effective Retail Competition

- Amended Substitute Senate Bill 3 (SB 3) did not anticipate that efforts to enable effective competition in the electric industry would still be unsuccessful in 2007.
- Today's circumstances highlight the gap in SB 3. The law assumes that there is effective competition in the supply of retail generation service while sustained reality confirms that this is not the case. The law as enacted in 1999 and applied since leaves Ohio poorly equipped to deal with the current circumstances.
- The gap in Ohio's restructuring law is being used by some stakeholders to threaten Ohio with excessive and volatile prices or to work against the objectives established by the General Assembly (see attached Section 4928.02, ORC). Over customers' protests, the PUCO has held that it does not have the ability to impose a rate stabilization plan on a utility (the Mon Power story).
- The gap is promoting litigation and making utility and customer capital investment more difficult, more risky and more expensive. Capital investment is essential if Ohio wants to renew its manufacturing strengths.
- Ohio must fill the gap created by SB 3 if it wants to effectively deal with the real world conditions that are inflicting substantial pain and suffering in the states (Maryland, Illinois, Montana, New Jersey, Pennsylvania) that continue to authorize "market prices" where there is no effective competition.
- Our quest does not require a polarizing choice between "regulation" and

"competition". It does not ask Ohio's leaders to return to a search for an energy policy or invite a debate over how many "incentives" customers must pay before Ohioans have access to reliable service and reasonable rates. We call on Ohio's leaders to take action with the understanding that SB 3, as designed and applied, created a gap that leaves Ohio without the tools it needs to deal with current conditions. This gap hurts all stakeholders.

Objective 2: Restore/Confirm Economic Development/Retention Tools

- SB 3 did not remove the special arrangement option used for decades to provide energy-intensive businesses with customized electric service arrangements.
- When Ohio's businesses looking to expand or maintain operations in Ohio inquire about the availability of special arrangements, Ohio's utilities respond with an interpretation of SB 3 that finds that customized arrangements are illegal.
- Right or wrong, this interpretation of SB 3 chills interest in maintaining and expanding operations in Ohio and leaves Ohio without an important economic development/retention tool.
 - Today, this tool could be used to encourage distributed generation where it can efficiently work to accomplish reliability (operating and planning) or least cost objectives. It can also be applied to support least cost investment in equipment that permits fuller utilization of existing capacity while reducing emissions.
- If Ohio ensures that the utilities that help to effectively use this tool are not being harmed, the utilities' interests will be

better aligned with Ohio's development/retention objectives.

- As in the past, Ohio controls the availability of special arrangements. Ohio can manage the tool so that it does not harm other stakeholders.

Objective 3: Use State Authority to Facilitate Capital Formation/Investment that Promotes Sustainable Energy Security

- SB 3 assumed that an effective electric market would be in place by mid-2003 and be functioning efficiently to meet reliability (planning and operating) and environmental objectives. This assumption is not supported by the experience since SB 3 was enacted.
- When Ohio's incumbent suppliers offer to provide capital for infrastructure investment, they use their default supplier obligation to demand "incentives" or guarantees for projects without performance accountability. The guarantees are measured against a capitalization ratio that includes common equity even though the proposals require customers to assume the project's financial and business risk. These demands hold Ohio hostage to choices that are not framed based on Ohio's policy objectives or consumers' interests.
- New generating or transmission capacity funded by forced investment by customers is subject to control by the Federal Energy Regulatory Commission (FERC) and regional transmission organizations (RTOs). Proposals that require Ohio customers to underwrite these projects create an equity imbalance because FERC and RTOs can direct the "benefits" to customers outside Ohio. An Ohio energy authority may provide Ohio with greater ability to control its own destiny and to resist federal results that work against Ohio's energy goals.

- There is no Ohio vehicle to facilitate coordinated capital investment by Ohio's investor-owned, munis and coop utilities.
- If Ohio customers are going to carry risk associated with capital investment required to retain and expand capacity and make non-bypassable payments to fund these efforts, a properly run state energy authority could work to lower the cost of this burden, ensure that benefits follow the burden and facilitate public-private partnerships focused on a balanced mix of supply and demand side resources that promote Ohio's objectives.

Objective 4: Don't Make Things Worse by Feeding FERC's Consumer Unfriendly RTOs

- FERC and its RTO agents are pushing physical and commercial theories that are not aligned with consumers' needs or the law of physics. These federal entities promote actions that raise prices, increase volatility and fail accountability tests. FERC and the RTOs "stay the course" despite repeated protests by customers and utilities. The potential for damage to ultimate customers and state economies increases as FERC and the RTOs leap to "Day 2" configurations.
- Contrary to its early claims, FERC made participation in RTOs voluntary.
- SB 3 requires the PUCO to determine if RTO elections by electric utilities are appropriate in light of Ohio's policy and specific criteria.
- The PUCO should use its existing authority proactively to limit recovery of RTO-related costs to "Day 1" costs (which are tied to reliability objectives) unless and until an electric utility demonstrates by clear and convincing evidence that the benefits to consumers exceed the costs.

Section 4928.02, Ohio Revised Code — Ohio's Electric Policy.

It is the policy of this state to do the following throughout this state beginning on the starting date of competitive retail electric service:

- (A) Ensure the availability to consumers of adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service;
- (B) Ensure the availability of unbundled and comparable retail electric service that provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs;
- (C) Ensure diversity of electricity supplies and suppliers, by giving consumers effective choices over the selection of those supplies and suppliers and by encouraging the development of distributed and small generation facilities;
- (D) Encourage innovation and market access for cost-effective supply- and demand-side retail electric service;
- (E) Encourage cost-effective and efficient access to information regarding the operation of the transmission and distribution systems of electric utilities in order to promote effective customer choice of retail electric service;
- (F) Recognize the continuing emergence of competitive electricity markets through the development and implementation of flexible regulatory treatment;
- (G) Ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa;
- (H) Ensure retail electric service consumers protection against unreasonable sales practices, market deficiencies, and market power;
- (I) Facilitate the state's effectiveness in the global economy.

Report to the House of Representatives, Select Committee to Study Ohio's Energy Policy, October 15, 2003. (a quote from page 3)

As Ohio treaded into uncharted waters by being one of the first states to deregulate its electric utility industry, the General Assembly knew that regulation and oversight by the PUCO would be necessary to achieve a competitive market. The legislature gave the PUCO a tremendous amount of supervision and management authority in SB 3, and it continues to monitor the market as we move through the transition periods. For example, to give competition more time to develop, the PUCO approved an extension of the transition period for Dayton Power & Light. Consumer advocates, regulatory officials and industry representatives worked together to craft a new plan, agreed to by the parties, to continue the framework of a competitive market while allowing some protection to customers. **The members encourage the PUCO to continue to take the necessary steps, whether by rule or a request for legislation, to ensure that a healthy competitive market is in place before full competition begins.** Ohio has been a model to the rest of the county regarding its innovative and vanguard approach to the electric utility industry. By continuing to design good public policy to shape the industry, Ohio can remain a prosperous, growing state through the 21st Century.