**BEFORE**
**THE PUBLIC UTILITIES COMMISSION OF OHIO**

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| In the Matter of the Review of the Power Purchase Agreement Rider of Ohio Power Company for 2018. | )<br>)<br>)<br>) | Case No. 18-1004-EL-RDR |
| In the Matter of the Review of the Power Purchase Agreement Rider of Ohio Power Company for 2019. | )<br>)<br>) | Case No. 18-1759-EL-RDR |

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# DIRECT TESTIMONY OF JOHN A. SERYAK ON BEHALF OF THE OHIO MANUFACTURERS' ASSOCIATION ENERGY GROUP

**(PUBLIC VERSION)**

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**December 29, 2021**

## I. INTRODUCTION

**Q1. Please state your name and business address.**

A1. My name is John A. Seryak. My principal place of business is at 5701 N. High Street, Suite 112, Worthington, Ohio 43085.

**Q2. By whom are you employed and in what capacity?**

A2. I am the lead analyst at RunnerStone, LLC (RunnerStone) on energy regulatory, policy, and market matters. I am also Chief Executive Officer of Go Sustainable Energy, LLC (Go Sustainable Energy), a consultancy that provides technical assistance on energy technology and energy management matters to the industrial, commercial, residential, and utility sectors. Runnerstone is a wholly owned subsidiary of Go Sustainable Energy.

**Q3. On whose behalf are you testifying in this proceeding?**

A3. My testimony is being sponsored by the Ohio Manufacturers' Association Energy Group (OMAEG). OMAEG is a non-profit entity that strives to improve business conditions in Ohio and drive down the cost of doing business for Ohio manufacturers. OMAEG members take service under transmission, sub-transmission, primary, and secondary electric rate schedules.

**Q4. Please describe your professional experience and qualifications.**

A4. I received a Bachelor's degree in Mechanical Engineering and a Master's of Science degree in Mechanical Engineering from the University of Dayton. I am a licensed Professional Engineer in the state of Ohio. I have worked extensively on energy matters for twenty years. My experience includes fieldwork at industrial, commercial, and residential buildings, identifying energy savings opportunities and quantifying the energy and dollar savings. This experience has been for the last fifteen years chiefly through my responsibilities as the founding partner of Go Sustainable Energy. Finally, I have eight years of experience in regulatory and policy analysis in the energy industry. In connection with these experiences, I have authored or co-authored over thirty peer-reviewed academic papers on technical, programmatic, cultural, and regulatory issues concerning energy resources.

**Q5. Have you participated in proceedings before the Public Utilities Commission of Ohio (PUCO) previously?**

A5. Yes, I have provided testimony and advised clients on numerous energy-related issues before the PUCO, including:

- *In the Matter of the Review of the Reconciliation Rider of Duke Energy Ohio, Inc.*, Case No. 20-167-EL-RDR;
- *In the Matter of the Long-Term Forecast Report of AEP Ohio and Related Matters,* Case No. 18-0501-EL-FOR*;*
- *In the Matter of the Application of the Ohio Power Company for Authority to Establish a Standard Service Offer*, Case No. 16-1852-EL-SSO*;*
- *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company For Approval of Their Energy Efficiency and Peak Demand Reduction Program Portfolio Plans for 2017 through 2019*, Case No. 16-0743-EL-POR:
- *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Power Purchase Agreement for Inclusion in the Power Purchase Agreement Rider*, Case No. 14-1693-EL-RDR;
- *In the Matter of the Application of AEP Ohio, Inc., for Approval to Continue Cost Recovery Mechanism for Energy Efficiency Programs through 2016*, Case No. 14-1580-EL-RDR;
- *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and the Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 14-1297-EL-SSO; and,

- *In the Matter of the Application of AEP Ohio, Inc., for Recovery of Program Costs, Lost Distribution Revenue and Performance Incentives Related to its Energy Efficiency and Demand Response Programs*, Case No. 14-0457-EL-RDR.

## II. OVERVIEW AND CONCLUSIONS

**Q6. What is the purpose of your testimony in this proceeding?**

A6. My testimony addresses the PUCO's prudency review of Ohio Power Company's (AEP Ohio) Power Purchase Agreement Rider (Rider PPA) during the audit period, and the prudency and performance audit conducted by London Economics International, LLC (LEI). The PUCO approved AEP Ohio's Rider PPA as a rate stabilization charge, with certain charges recoverable from ratepayers, subject to an annual prudency review.[1] Specifically, based upon my regulatory analysis and expertise, and, at a minimum, I recommend that the PUCO make the following findings:

- that the $[redacted] collected through Rider PPA associated with debt repayment, debt interest, and profit should be disallowed and refunded to customers, as these costs are not part of a market cost or market revenue stream, and, therefore, cannot act as a rate stabilization charge or a financial hedging mechanism;
- that the $4,846,196 collected for above-market priced coal is imprudent and unreasonable and should be disallowed and refunded to customers;

[1] *In re Ohio Power Co.*, Case Nos. 13-2385-EL-SSO, et al. (ESP III Case), Opinion and Order at 25 (February 25, 2015).

- that Rider PPA as implemented by AEP Ohio is neither functioning as a financial hedge nor a rate stabilization charge. And therefore, the costs collected through Rider PPA during the audit period are unreasonable, imprudent, and not in customers' best interests and should be disallowed in their entirety and refunded to customers; and,
- that the appropriate standard for the PUCO to use is what is in the best interest of customers. This standard should be applied to the prudency review as what is in the best interest of customers is the whole purpose for implementing a rate stabilization charge and the consideration of whether a charge to customers is reasonable or unreasonable.

Although the LEI audit is very broad, my recommendations are narrow, concentrating on a limited number of issues. Accordingly, absence of a comment on my part regarding a particular aspect of the LEI audit does not signify agreement or disagreement with that aspect of the audit report. I also reserve the right to offer comment on other issues covered in this LEI audit or other audits related to AEP Ohio's recovery of costs associated with the Ohio Valley Electric Corporation (OVEC) power plants.

## III. <u>HISTORY</u>

**Q7. Has the PUCO directly addressed whether an OVEC-only based PPA is reasonable?**

A7. Yes. In AEP Ohio's third electric security plan (ESP III), AEP Ohio requested approval for Rider PPA as a rate stabilization charge, consisting at the time of only net costs associated with AEP Ohio's entitlement to electricity output from OVEC.[2] In its February 25, 2015 Order in AEP Ohio's ESP III Case, the PUCO found that a rate stabilization charge was lawful, but also found that an OVEC-only rate stabilization charge was unreasonable and denied AEP Ohio the authority to recover net costs associated with OVEC in Rider PPA.[3] Accordingly, the PUCO approved Rider PPA but set the rider at $0.[4]

The PUCO's Order expressly contemplated whether an OVEC-only Rider PPA was reasonable and stated, "we next consider, based on the record evidence, whether AEP Ohio's PPA rider proposal is *reasonable* and whether customers would, in fact, sufficiently benefit from the rider's financial heading mechanism."[5]

In denying AEP Ohio authority to recover costs through an OVEC-only Rider PPA the PUCO stated, "the Commission agrees …that the evidence of record reflects that the rider may result in a net cost to customers, with little offsetting benefit from the rider's intended purpose as a hedge against market volatility."[6] The PUCO's ESP III Order further emphasized that an OVEC-only based PPA is unreasonable: "we are not persuaded that the PPA rider proposal put forth by AEP Ohio in the

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[2] *Id.* at 8.

[3] *Id.* at 25.

[4] *Id.*

[5] *Id.* at 23 (emphasis added).

[6] *Id.* at 24.

present proceedings would, in fact, promote rate stability, as the Company claims, or that it is in the public interest."[7]

**Q8. Why did the PUCO subsequently approve AEP Ohio's request to recover costs through Rider PPA?**

A8. The PUCO subsequently approved cost recovery through Rider PPA in a proceeding in which AEP Ohio proposed to create a rate stability charge by recovering net costs of multiple generating units, including OVEC but not limited to OVEC, and which included renewable energy projects.[8] In regards to the newly proposed Rider PPA, the PUCO stated: "we find that the record in these proceedings demonstrates a projected net credit to customers of $37 million over the current ESP term through May 31, 2018, or $214 million through May 31, 2024, under the term of the PPA rider."[9]

Accordingly, the PUCO's approval of cost recovery through Rider PPA resulted from two important differences when compared to AEP Ohio's first request in its ESP III case: 1. Rider PPA was not solely tied to OVEC, and 2. Rider PPA was

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7 *Id.*

8 *In re Ohio Power Co.*, Case Nos. 14-1693-EL-RDR, et al. (Rider PPA Case), Opinion and Order at 21-22; 42-44 (March 31, 2016),

9 *Id.* at 77.

expected to yield a net credit to customers through May 31, 2018 and a larger net credit through May 31, 2024, not a net cost.

It should be noted that even in the prior case, intervening parties disagreed with AEP Ohio's forecast that Rider PPA would yield a net credit.[10] The PUCO responded by qualifying its ruling, stating, "we agree that a rate stability proposal, such as the PPA rider, must not impose unreasonable costs on customers."[11] The PUCO further emphasized that its approval of cost recovery through Rider PPA was conditioned on resulting credits to customers. Importantly, the PUCO stated: "[a]gain, we base our decision approving the PPA rider today on AEP Ohio's projection that is predicted to result in a net credit of $214 million."[12]

**Q9. Did the PUCO's orders on Rider PPA establish parameters for what constitutes "reasonable costs" that can be passed onto customers through a rate stability mechanism, such as Rider PPA?**

A9. Yes. In initially denying cost recovery for OVEC-only costs through Rider PPA, the PUCO specifically stated that the collection of OVEC-only costs would be unreasonable if Rider PPA was expected to result in charges to customers.[13] The PUCO subsequently approved cost recovery through Rider PPA when AEP Ohio proposed to include additional power plants than just OVEC, including renewable

[10] See, e.g., *id.* at 63-65.

[11] *Id.* at 78.

[12] *Id.* at 81.

[13] ESP III Order at 23 (February 25, 2015).

energy projects, in the hedging mechanism, which was expected to result in credits to customers.[14]

**Q10. Were there further modifications to Rider PPA?**

A10. Yes. On November 3, 2016, the PUCO issued another order in the Rider PPA Case wherein the PUCO approved a modified version of Rider PPA, which comprised of costs and revenues associated with OVEC plus the costs and revenues associated with up to 900 MW of potential renewable energy generation.[15] This order was the result of AEP Ohio stating on rehearing that it no longer wished to include costs and revenues associated with its affiliates' other coal plants in the PPA recovery mechanism, citing Federal Energy Regulatory Commission (FERC) issues.[16]

Additionally, approval for cost recovery under the Rider PPA mechanism was part of a broader settlement package that contained other settlement provisions unrelated to the PPA.[17] The PUCO cited these other settlement provisions as a reason to approve an amended Rider PPA, stating, "[i]n order to preserve the

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[14] Rider PPA Case, Order at 63-65; 77 (March 31, 2016).

[15] Rider PPA Case, Second Entry on Rehearing at 6 (November 3, 2016).

[16] *Id.* at 23.

[17] *See* Rider PPA Case, Order at 23-45 (March 31, 2016).

customer benefits of the stipulation, we approve AEP Ohio's request to modify the stipulation…."[18]

The PUCO also relied on forecasts of customers receiving credits under the Rider PPA mechanism, stating that "the stipulation's PPA rider proposal as modified now to include only the OVEC PPA, is projected to provide ratepayers with a net credit of approximately $110 million."[19] At this point, Rider PPA still included potential renewable energy projects.

In the November 3, 2016 order, the PUCO further stated that "the rider which will include OVEC PPA and potentially a number of renewable energy PPAs in the future, will provide a rate stability benefit…."[20]

Lastly, the PUCO emphasized that it may modify its ruling on reasonableness of a rate stability charge if the net cost estimates in the record change: "[t]he Commission emphasized, no less than four times, that its decision in the ESP III Case was based on the record before it."[21] And it also stated: "we find that our approval today of the PPA rider with the OVEC PPA alone is based on a different

[18] Rider PPA Case, Second Entry on Rehearing at 2 (November 3, 2016).

[19] *Id.* at 31.

[20] *Id.* at 32.

[21] *Id.* at 30

set of facts and circumstances, as well as distinct evidentiary record, and is, thus not inconsistent with our prior decision in the ESP [III] Case."[22]

**Q11. Did the PUCO's subsequent orders on Rider PPA further clarify what constitutes reasonable costs in a rate stability mechanism, such as Rider PPA?**

A11. Yes. The PUCO reinforced the rationale expressed in its prior orders that Rider PPA must not only include costs associated with OVEC if it results in net costs to customers. It approved this version of Rider PPA envisioning that the rate stability mechanism would include costs associated with up to 900 MW of renewable energy at some point in the future.[23] Additionally, the PUCO approved this version of Rider PPA assuming it would result in net credits to customers.[24]

Importantly, the PUCO clarified that it can modify its approval of Rider PPA based on the record at the time. The PUCO specifically noted that the reason it was changing course from its decision in the ESP III Case was based on "a different set of facts and circumstances."[25]

**Q12. Has the PUCO made any other modifications to Rider PPA?**

A12. Yes. In AEP Ohio's ESP IV Case, the PUCO authorized cost recovery through Rider PPA to be divided into two riders, Rider PPA and the Renewable Generation

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[22] *Id.* at 31.

[23] *Id.* at 133.

[24] *Id.* at 207.

[25] *Id.* at 31.

Rider (Rider RGR).[26] This authority, however, did not modify the PUCO's previous rulings, which approved cost recovery for OVEC AND up to 900 MW of renewable energy through Rider PPA, or the PUCO's assumptions that Rider PPA as constructed would result in customer credits during the audit period and after.

**Q13. Were there any additional modifications to the facts and circumstances surrounding the approval of Rider PPA?**

A13. Yes. The potential 900 MW of renewable energy generation was never included in Rider PPA, as AEP Ohio failed to demonstrate need to include this generation.[27]

[26] *In re Ohio Power*, Case Nos. 16-1852-EL-SSO, et al. (ESP IV Case) Opinion and Order at 20-22, 104-105 (April 25, 2018).

[27] *In the Matter of the Application of Ohio Power Company for Approval to Enter into Renewable Energy Purchase Agreements For Inclusion in the Renewable Generation Rider*, Case Nos. 18-1392-EL-RDR, et al., Opinion and Order at ¶ 128 (November 21, 2019).

Additionally, the costs associated with OVEC passed through Rider PPA failed to yield a net credit to customers as projected and anticipated by the PUCO.

## IV. THE CURRENT "OVEC-ONLY" RIDER PPA THAT RESULTS IN NET COSTS TO CUSTOMERS IS UNREASONABLE AND IMPRUDENT

**Q14. Has the PUCO ever approved the reasonableness or prudency of costs passed through Rider PPA associated with OVEC?**

A14. No.

**Q15. Has the PUCO ever approved the reasonableness or prudency of costs passed through a rate stability mechanism that only resulted in net costs to customers?**

A15. No.

**Q16. Could you describe Rider PPA as currently constructed considering the PUCO's prior rulings?**

A16. Rider PPA currently recovers net costs associated with the two OVEC generating plants, one of which is located in Indiana. According to the LEI audit, during the audit period, AEP Ohio charged customers $[redacted] in 2018 and $[redacted] in 2019 for costs associated with the OVEC plants, totaling $[redacted].[28] Rider PPA did not result in net credits to customers during the audit period. A rate stability mechanism, such as Rider PPA, that results in net costs to customers is not just and reasonable and creates a similar set of facts and circumstances that led to

[28] LEI Audit Report (Confidential) at 28.

the PUCO originally denying AEP Ohio cost recovery for costs associated with OVEC through Rider PPA in AEP Ohio's ESP III Case.[29]

As indicated above and in the prior PUCO orders, a rate stability mechanism that only results in net costs to customers and that collects costs associated with only the OVEC plants was not neither part of the record nor envisioned by the PUCO. In fact, the last approval of a rate stability mechanism construct by the PUCO for AEP Ohio  included up to 900 MW of renewable energy generation.[30]

Additionally, and importantly, the PUCO approved cost recovery for AEP Ohio through Rider PPA on the assumption that Rider PPA would yield credits to customers during the audit period.[31]

**Q17. Based on your regulatory expertise and industry experience, what actions do you recommend that the PUCO take in order to protect customers against unreasonable or imprudent costs included in Rider PPA during the audit period?**

A17. Based on my regulatory expertise and industry experience, given that Rider PPA has not resulted in credits to customers during the audit period as envisioned, I recommend that the PUCO disallow all costs included in Rider PPA during the audit period as unreasonable and imprudent. The PUCO has made it clear that it

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[29] *See* ESP III Case, Opinion and Order at 23-24 (February 25, 2015).

[30] *See* ESP IV Case, Opinion and Order at 20-22, 104-105 (April 25, 2018).

[31] *See* Rider PPA Case, Opinion and Order at 77 (March 31, 2016).

may disallow OVEC-related costs in Rider PPA based on "facts and circumstances" in the record. Additionally, as explained above, the PUCO previously determined that including costs in Rider PPA that are associated with only the OVEC plants and that result in net costs to customers is unreasonable and imprudent, and such costs should be disallowed through a prudency review. Since approval of Rider PPA, two important underlying facts have changed, making the costs unreasonable and imprudent during the audit period: renewable energy was not included in the hedging mechanism for rate stability, and the OEC-only costs resulted in charges to customers during the audit period.

Accordingly, the PUCO should maintain consistency with its prior rulings and disallow the collection of unreasonable and imprudent costs from customers during the audit period, and the PUCO should refund all monies improperly collected from customers.

## V. <u>OTHER UNREASONABLE AND IMPRUDENTLY INCURRED COSTS DURING THE AUDIT PERIOD SHOULD BE DISALLOWED</u>

**Q18. Were there any other unreasonable costs or imprudently incurred costs collected through Rider PPA during the audit period?**

A18. Yes. As discussed further below, OVEC paid unreasonable, significantly above-market prices for coal from Resource Fuels, a Columbus, Ohio based coal company.[32] These imprudently incurred costs should be disallowed.

[32] *See* Table 1. US EIA 923 Data: Clifty Creek Coal Purchases, https://www.eia.gov/electricity/data/eia923/.

LEI auditors have determined that OVEC's Clifty Creek unit paid above-market prices for coal, and "recommend[ed] [that]OVEC negotiate with the coal suppliers to ensure the delivery of coal with good quality but at more competitive prices."[33]

It is not clear to me why LEI did not include a similar finding in its audit report in this case regarding AEP Ohio's Rider PPA. LEI should have determined that the coal purchases by OVEC that were recovered through Rider PPA were excessive, unreasonable, and resulted in imprudently incurred costs that should be disallowed. There is no justification for OVEC purchasing the coal at above-market prices and incurring such unreasonable costs. According to OVEC's reports to the US Energy Information Administration, the heating content of this above-market priced coal is the same as other coal that OVEC's Clifty Creek purchases at lower prices, from the same mine, but from a different company.[34]

To clarify, OVEC's Clifty Creek purchased coal from the same mine, with the same energy content, from two different companies. It is essentially the same coal. But one company charged $56-57 /million Btu, while another company charged $41-47 /million Btu. I present this publicly available data in Table 1.

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[33] *In the Matter of the Review of the Reconciliation Rider of Duke Energy Ohio, Inc.*, Case No. 20-167-EL-RDR. Rider PSR Audit Report at 64, 71 (October 21, 2020).

[34] *See* Table 1. US EIA 923 Data: Clifty Creek Coal Purchases, https://www.eia.gov/electricity/data/eia923/.

| | 2018 | | 2019 | |
|---|---|---|---|---|
| Mine | River View Mine | | | |
| Supplier | Alliance Coal | Resource Fuels | Alliance Coal | Resource Fuels |
| Energy Content (million Btu/unit) | 23.05 | 23.03 | 23.06 | 23.01 |
| Coal Purchase (units) | 1,330,482 | 999,622 | 1,595,914 | 999,739 |
| Coal Price (cents/million Btu) | 181.01 | 244.14 | 205.99 | 249.06 |
| Coal Price ($/unit) | $ 41.72 | $ 56.24 | $ 47.50 | $ 57.31 |
| Above-market Coal Payments ($) | | $ 14,509,675 | | $ 9,806,412 |
| Total Above-market Coal Payments ($) | | | | $ 24,316,087 |
| AEP Ohio Share of Above-market Coal Payments ($) | | | | $ 4,846,196 |

Table 1. US EIA 923 Data: Clifty Creek Coal Purchases

During the audit period, OVEC purchased 1,999,361 units of the over-priced coal. As compared to the price charged by another company, OVEC over-paid by $24,316,087 for comparable coal from the same coal mine. AEP Ohio's share of this overpayment, based on its 19.93% entitlement to OVEC's available energy output is $4,846,196.

**Q19. Do you have a recommendation regarding the Clifty Creek coal purchases?**

A19. Yes, I recommend that the PUCO disallow the excessive costs associated with the coal purchased at above-market prices from the one company as an unreasonable and imprudent cost that is not in customers' best interests. LEI found as such, but failed to include a recommendation in the AEP Ohio audit report to disallow such imprudently incurred costs.

**Q20. Were there other costs collected through Rider PPA in 2018 and 2019 that were unreasonable and imprudent?**

A20. Yes, AEP Ohio collected unreasonable and imprudently incurred costs through Rider PPA during the audit period, such as debt and interest payments for OVEC and OVEC shareholder profits.

**Q21. Why are debt and interest payments an unreasonable cost to include in Rider PPA and collect from customers?**

A21. Debt and interest payments are fixed costs that do not impact electricity market prices and have no relation to how much revenue a power plant generates in the electric market. Accordingly, costs associated with debt and interest payments should not be included as part of a rate stabilization charge and passed onto customers.

Even if OVEC were to shut down completely and have no market revenue or costs, AEP Ohio would still be obligated to make these debt and interest payments. In other words, the cost of debt are not part of a wholesale electric market transaction, and therefore are not and should not be part of a market hedge.

**Q22. Does AEP Ohio include debt and interest payments as a cost in its market bids?**

A22. [redacted].

[35] LEI Audit Report (Confidential) at 48-51.

**Q23. What is the cost of capacity used in a wholesale capacity market transaction?**

A23. The cost of capacity in a wholesale capacity market transaction is the resource's bidding price multiplied by the incremental bid capacity. In the case of AEP Ohio's OVEC capacity entitlement, the cost of capacity in the transaction is the bid price that AEP Ohio submits to the PJM base residual auction (BRA) multiplied by the capacity bid in Megawatts.

**Q24. How should an electricity resource price its capacity offers?**

A24. A resource should set its capacity bid price to cover operating costs net of its energy and ancillary market revenue. Operating costs include costs such as operations, staff, and maintenance. Operating costs do not include costs like debt or interest expenses, as those are sunk costs. This is an economically rational way to price capacity bids, as described in The Electricity Journal article "Forward Capacity Market CONEfusion."[36] It is generally referred to as net going-forward cost.

For example, it is not economically rational for a resource to bid below its net going-forward cost because the resource could clear while being paid a price that does not cover its operational costs, thus incurring losses. However, it is not economically rational to bid above the net going-forward cost either as this risks the market clearing below the bid price but above the net going-forward cost,

[36] J. Wilson, "Forward Capacity Market CONEfusion" The Electricity Journal. November 2010, Vol. 23, Issue 9. Pg 3 and 16 of PDF: http://wilsonenec.com/dev/wp-content/uploads/2016/07/Capacity-Market-CONEFusion-Elec-Journal-as-posted.pdf (stating, "[p]ower plant's net going-forward cost is the cost it must incur to operate in a year with a capacity obligation, net of anticipated market earnings, and could avoid if not operating with a capacity obligation. In principle, if a plant cannot receive this amount from the capacity market, the owner should find it more attractive to shut down for the year or to sell the plant's output into an adjacent region than to operate with the capacity supply obligation.").

resulting in missed operating profits. Therefore, the price of a resource's capacity bid should account for operating costs net of energy and ancillary revenue, but not the cost of debt, interest on debt, or shareholder profits.

The capacity market settlement price is a signal to the resource on whether its debt, interest, and profits can be recovered in the wholesale markets. If a resource does not clear the capacity market consistently and cannot cover its operating costs, it should consider shutting down or selling to a different operator. If a resource clears the market consistently but cannot cover its debt payments, it must consider renegotiating its debt. To the point, the cost of a resource's capacity in a wholesale market transaction should not include debt payments, interest payments, or shareholder profits.

**Q25. If it is not economically rational for electric market bidders to include debt and interest as a cost in its market bids, should AEP Ohio include it as a retail cost in Rider PPA?**

A25. No. The PUCO stated in its order approving cost recovery through Rider PPA that "[r]etail cost recovery may be disallowed as a result of the annual prudency review if the output from the units was not bid in a manner that is consistent with participation in a broader competitive marketplace comprised of sellers attempting to maximize revenues."[37] Thus, since rational bidders in the competitive marketplace do not account for their debt and interest costs in their market bids, AEP Ohio also should not be authorized to include OVEC's debt and interest costs

[37] Rider PPA Case, Order at 89 (March 31, 2016).

as part of the costs recovered through Rider PPA. Because OVEC cannot cover its debt and interest payments with market revenue, AEP Ohio should act in a manner consistent with the broader competitive marketplace, which would be to seek to renegotiate its debt obligation with its creditors. As such, any costs associated with debt and interest payments or shareholder profits during the audit period should be disallowed.

**Q26. Is AEP Ohio using Rider PPA as an electric market hedge for customers?**

A26. No. AEP Ohio is using Rider PPA as a debt payment vehicle to recoup all of its costs associated with OVEC. If OVEC's operations were truly being used as a financial hedge for customers, then OVEC's electricity market earnings should flow through to customers as credits. Debt payment for OVEC is the responsibility of AEP Ohio's shareholders, *not* AEP Ohio's customers. In fact, AEP Ohio's debt payment obligations to OVEC are not part of AEP Ohio's entitlement to OVEC's energy and capacity [redacted]. AEP Ohio's debt payment obligation to OVEC is a relatively fixed and sunk cost that cannot stabilize rates and should not be part of a rate stability mechanism.

**Q27. What is AEP Ohio's Share of the Debt and Interest Payments, and Shareholder Profits that were recovered in Rider PPA during the audit period?**

A27. The LEI audit report did not identify OVEC debt and interest payments for each month of the audit period, but instead selected a 6-month sample.[38] However, all twelve months of OVEC's debt payments in 2019 are available in another LEI audit report and can be used for the calculation. Table 2 presents the monthly debt payments, with estimates for unavailable months. Table 2 also presents a summary total of AEP Ohio's share of OVEC's debt and interest payments and shareholder

[38] *See* LEI Audit Report, Figure 10, Column A.

profits for these months. Italicized months are estimates of debt, interest, and deprecation, based on the average of available 2018 data.

I estimate that AEP Ohio paid $[redacted] for OVEC's debt, interest, and depreciation, and another $[redacted] towards shareholder distributions.

[redacted]

Table 2. OVEC's Debt and Interest Costs and Shareholder [redacted] and AEP Ohio's Share of These Costs (Confidential).

**Q28. What Capacity Pricing Did AEP Ohio Bid into the PJM BRA?**

A28. Section 5.3.6 of the LEI audit report describes AEP Ohio's bidding strategy. AEP Ohio did not [redacted]. AEP Ohio's OVEC capacity bid price for the 2018/19 auction was $[redacted], which had a clearing price of $164.77 /MW-day. AEP Ohio's OVEC capacity bid price for the 2019/20 auction was $[redacted] which had a clearing price of $100 /MW-day. LEI states that AEP Ohio's offer price was "[redacted]."[39]

The audit report did not identify AEP Ohio's offer price for the 2017/2018 delivery year.

**Q29. Are there other reasons that debt, interest, and shareholder profit should be disallowed as an unreasonable cost?**

A29. Yes. The PUCO should consider that a prior PUCO order limits recoverable costs associated with OVEC through a retail stability charge to "the net amount resulting from transactions, in the wholesale market, relating to [an Ohio electric distribution utility's (EDU)] entitlement under the Inter-Company Power Agreement (ICPA)."[40] The PUCO clarified that the rate stability mechanism "shall be effective with energy and capacity delivered to [an EDU] under the ICPA."[41] Therefore, the

[39] LEI Audit Report (Confidential) at 39.

[40] ESP IV Case, Stipulation and Recommendation at 18 (April 13, 2018) (ESP IV Settlement).

[41] *Id.*

PUCO previously authorized one Ohio EDU to recover costs through its rate stability mechanism that were netted from wholesale energy or capacity market transactions. Costs that do not net from a wholesale energy or capacity market transaction were not allowed to be collected through the rate stability mechanism. Given that AEP Ohio's Rider PPA is functionally similar to other EDU's rate stability mechanism with respect to the collection of costs associated with OVEC, Rider PPA should also only be authorized to recover net costs resulting from wholesale market transactions.

**Q30. Does AEP Ohio collect costs through Rider PPA that are not part of a wholesale energy or capacity market transaction?**

A30. Yes. By reviewing the data, it is clear that AEP Ohio did not [redacted] were not part of a wholesale market transaction, [redacted] and thus cannot be included as a recoverable cost that is authorized to be collected through Rider PPA.

Additionally, according to the ICPA, sponsoring companies are required to pay the debt obligation no matter if the company takes entitlement to the available power.[42] Thus, debt repayment is not related or resulting from a wholesale energy or capacity transaction and, thus, should be disallowed as it is not part of a market hedging strategy.

## VI. CONCLUSION

**Q31. What are your conclusions and recommendations?**

A31. I conclude that the recovery of all of the net costs associated with AEP Ohio's contractual entitlement in OVEC through Rider PPA is unjust, unreasonable, and imprudent. I also conclude that costs collected from customers through Rider PPA that are not a financial hedge should be disallowed, and that imprudent coal purchases should also be disallowed. Specifically, I recommend the following:

- At a minimum, the PUCO find that the $4,846,196 collected for above-market priced coal was imprudent and unreasonable and be disallowed and refunded to customers.

[42] ICPA at Section 9.181, https://www.sec.gov/Archives/edgar/data/73986/000000490406000041/x10a2.htm.

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- At a minimum, the PUCO find that the $[redacted] collected through Rider PPA associated with debt repayment, debt interest, and shareholder profit be disallowed and refunded to customers, as these costs are not part of a market transaction, and thus cannot act as a rate stabilization charge or a financial hedging mechanism.
- The PUCO find that Rider PPA as implemented by AEP Ohio is not functioning as a financial hedge, is thus not a rate stabilization charge, and that the costs collected by Rider PPA be disallowed in their entirety and refunded to customers.
- The PUCO determine that the standard that should be applied to a prudency review is what is in the best interest of customers. That standard is the whole purpose for implementing a rate stabilization charge and the consideration of whether a charge to customers is reasonable or unreasonable.

Taken together, the PUCO should disallow the collection of costs through Rider PPA and should order that all costs collected from customers through Rider PPA for the period of the audit (January 1st, 2018 through December 31st, 2019) be credited back to customers.

**Q32. Does this conclude your direct testimony?**

A32. Yes. However, I reserve the right to incorporate new information that may subsequently become available through discovery or otherwise.

## CERTIFICATE OF SERVICE

The Public Utilities Commission of Ohio's e-filing system will electronically serve notice of the filing of this document on the parties referenced on the service list of the docket card who have electronically subscribed to the case. In addition, the undersigned hereby certifies that a copy of the foregoing document also is being served via electronic mail on December 29, 2021 upon the parties listed below.

*/s/ Thomas V. Donadio*
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