



Ohio Environmental Council

Ohio Environmental Council's *Reply* Comments In the Matter of the OVEC Generation Purchase Rider Audits 21-0477-EL-RDR

Date: May 23, 2023

The Ohio Environmental Council joins the majority of commenters urging this Commission to schedule a hearing in this case. Ohio law requires a prudence *and* reasonableness review of costs passed to consumers by the Legacy Generation Rider.¹ Several of the utilities and stakeholders agree to three of the audit recommendations: increasing flexibility between must-run and economic commitments, reassessing coal inventories, and providing caps on capital expenditures. Where the utilities disagree with the audit findings, they fail their burden to show prudence and reasonableness.² OVEC had the information available to make prudent and reasonable decisions to limit costs and environmental impacts but stubbornly failed to act. Ohio ratepayers should not pay excessive fuel and operating costs, nor should they provide a return to OVEC for its poor decisions.

In their initial comments, the utilities largely argue the audit findings are irrelevant due to the existence of the Inter-Company Power Agreement (ICPA) or COVID-19 pandemic. However, AEP Ohio is amenable to the auditor's recommendations on fuel and operating costs. AEP Ohio and Duke also agree that allowing flexibility in the operation of OVEC between must-run and economic is a good idea. However, all of the utilities ask the PUCO to approve Component (D) costs, a return on equity, because the ICPA exempts Component (D) from a prudence review and this return goes to OVEC instead of them. Each of the utilities also argue that the unforeseen circumstances from COVID-19 exempt OVEC management decisions from

¹ R.C. 4928.148(A)(1).

² The utilities bear the burden to prove its costs are prudent and reasonable. "[I]f the evidence [is] inconclusive or questionable, the commission [can] justifiably reduce or disallow cost recovery." *In re Duke Energy Ohio, Inc.*, 131 Ohio St. 3d 487. The utilities must pass both hurdles of prudence and reasonableness before it can recover costs through the Legacy Generation Rider. R.C.4928.148(A)(1).

a prudence or reasonableness review. These arguments are a distortion of the prudence standard and post-hoc rationalizations.

The legislature specifically included a requirement that all costs be prudent *and* reasonable.³ Thus, this Commission must review all costs under both tests before allowing recovery. While the tests have some overlap, this Commission and the Ohio Supreme Court have traditionally evaluated them with two different purposes.

A prudence review looks at management's business decisions, and reasonableness adds an additional layer of public interest. A prudence review is a retrospective review into utility management decision making.⁴ Prudent decision making follows what a reasonable person would have done in light of conditions known or reasonably should have been known at the time the decision was made. *Id.* The PUCO has reviewed reasonableness under a burden to show operation and maintenance decisions provide a "benefit to ratepayers and the public interest."⁵ Thus a cost can only be prudent and reasonable if it was a sound decision based on the facts available at the time and the decision benefited the public interest.

While many of the utilities and stakeholders agree to work towards reducing costs and improving efficiency, many of the utilities' disagreements with auditor recommendations are post-hoc rationalizations and an attempt to stretch the scope of prudence and reasonableness. The OEC agrees with the Ohio Manufacturers' Association Energy Group that the mere existence of the ICPA, or its review by FERC, does not exempt it from the statutory requirement for the PUCO to conduct a prudency review. The statutory language in R.C. 4928.01(A)(42) applies to all "prudent costs." Costs such as Component (D) and excessive coal inventories are imprudent and unreasonable. Customers cannot foot the bill for these bad contracts.

I. Ohio law does not permit Ohioans to cover the costs of equity returns to any party.

All costs passed through the Legacy Generation Rider are subject to the limitation against collecting returns on investment. The fact that component (D) is a return on investment to OVEC does not exempt it from the limitations in R.C. 4928.01(A)(42). The exceptions in R.C. 4928.01(A)(42) including "any return on investment" modify all "prudently incurred costs." This exception applies to returns for any party. Even if component (D) was a prudent cost, it is still not reasonable. Ohio consumers should not be paying a return to OVEC.

³ R.C. 4928.148(A)(1).

⁴ *Cincinnati v. PUC*, 67 Ohio St.3d 523, 530, 620 N.E.2d 826, 830 (1993).

⁵ *See e.g., Ohio Consumers' Counsel v. PUC*, 110 Ohio St. 3d 394, 398 (evaluating reasonableness of stipulation requires showing a "benefit to ratepayers and the public interest"); *See also, In re Ohio Power PPA Rider*, Case No. 14-1693-EL-RDR, Opinion & Order (March 31, 2016) at 89 (burden of proof to show reasonableness of stipulation by showing it is "in the best interest of retail consumers.").

The statute defines “prudently incurred costs related to a legacy generation resource” as those “allocated pursuant to a power agreement approved by the federal energy regulatory commission that relates to a legacy generation resource... .”⁶ However, “such costs”—prudently incurred costs—exclude “any return on investment in common equity.” Thus, while a cost must be included in the ICPA in order to be recovered, that is only a threshold condition. “Such costs” are still subject to the exemptions in R.C. 4928.01(A)(42).

Even if the return on investment to OVEC is a prudently incurred cost, it is still not reasonable. There is no benefit to customers or to the public interest in providing OVEC with a return on investment for poorly run, dirty coal plants. These coal plants pollute Ohio air, jeopardizing the health of nearby residents, and are losing money. Nothing in the statutory language of R.C. 4928 intended to give OVEC a bonus for doing such a bad job that it required a taxpayer bailout.

Ohio law does not allow ratepayers to foot the bill for returns on investment to any party. Even if the definition of prudently incurred costs did not exclude returns on investment, such a cost would not be reasonable. The Commission must exclude this cost from recovery.

II. The over-inventory of coal is a longstanding issue at OVEC, and Ohioans should not pay these excessive costs.

Ohioans should not pay for poor choices in face of clear over supply and drops in demand. The utilities focus on the retrospective nature of a prudence test to argue that the only decision this Commission should review is the one to enter into the supply contracts several years ago. However, this is a misinterpretation of the prudence test, which does not require analyzing one single decision point and then indefinitely assuming prudence. The prudence test may involve analyzing several decision making points.⁷ Given that this audit covers 2020, the prudence test should analyze OVEC’s decisions for operating and maintenance covering 2020. The facts available to OVEC leading up to and throughout 2020 demonstrate its decision to maintain the same years-old fuel contract was imprudent.

A delivery contract that results in oversupply can be found imprudent, even if the company’s contract relied on fuel forecasting reports.⁸ In *Vectren*, the company entered into supply contracts, based on internal forecasting, that resulted in an oversupply of natural gas. The

⁶ R.C. 4928.01(A)(42).

⁷ See, e.g. *Office of Consumers' Counsel v. Public Utilities Com.*, 67 Ohio St. 2d 153, 166 (While the Court ultimately found the prudence test was the wrong test for determining rate base, it notes the Commission provided a prudence review of multiple decisions that went into constructing and abandoning plant construction).

⁸ *Vectren Energy Delivery of Ohio, Inc. v. PUC*, 113 Ohio St. 3d 180, 181.

Supreme Court found that even though the utility had used forecasting reports reviewed by the PUCO, “[t]he company's customers did not have to bear the cost of the oversupply....”⁹

Throughout a project, the Ohio Supreme Court will look at multiple decision points when evaluating prudence.¹⁰ In *Cincinnati Gas and Electric*, the company wanted to implement a new customer service system (CSS), and determined that it could complete the project in-house. However, the company faced several delays, setbacks, and increased costs before it decided to course correct and hire an outside firm to implement the system. The Court found that the costs of these delays could not be passed on to ratepayers because those costs were the result of the company’s own poor management decisions:

Institutional hubris is at the heart CG&E's problems with the development of the CSS. The stubborn belief that the project could be completed in-house, despite continued rising costs and missed deadlines, was the source of much of the project's expense. *Id.*

Each set back and increased cost was another decision point. Each time the company decided to move forward despite these setbacks, that decision was imprudent.

Here, the facts available to OVEC in 2020 required a reevaluation of its fuel supply contracts. Going into 2020, OVEC already faced an oversupply of coal. OVEC also knew that the demand for coal-fired energy was consistently decreasing as cleaner alternatives entered the market. As COVID-19 hit, all sectors of the economy faced uncertainty. Business leaders knew they would need to reassess their assumptions, including inventory forecasts. In fact, OVEC authorized a switch from a must-run to an economic availability status in PJM markets as a response to the pandemic conditions.¹¹ At this point, OVEC knew or should have known that its fuel forecasts were incorrect and could have tried to course correct.

OVEC had several options available to try to mitigate over supply. First, it could have attempted to renegotiate the contract. The utilities note that this would be difficult and potentially incur litigation costs. However, there is precedent to renegotiate these contracts. In 2009, the Ohio Power Company was receiving coal at much lower than market prices through a 20-year fuel supply contract.¹² The supplier forced it to renegotiate the contract which resulted in a settlement agreement and Ohio Power Company ultimately purchasing coal at a higher price.

⁹ *Id.*

¹⁰ *Cincinnati Gas & Elec. Co. v. PUC*, 86 Ohio St. 3d 53, 59.

¹¹ Initial Comments of Ohio Power Company in Response to the Audit Report, Case No. 21-0477, p. 4 (filed 5/8/2023).

¹² In re Fuel Adjustment Clauses for Columbus S. Power Co., 140 Ohio St. 3d 352.

OVEC could have done something similar here. At the very least, OVEC could have negotiated to defer some of these deliveries.¹³

OVEC's oversupply of fuel is an imprudent cost. The utilities' reliance on the COVID-19 pandemic as an unforeseen circumstance is in many ways a post-hoc rationalization for what was ultimately a poor contract. OVEC already knew it was facing an oversupply and its forecasting reports had been inaccurate. Instead of taking measures to mitigate this over forecasting, OVEC did nothing. Consumers should not pay for this poor management choice.

III. Conclusion

The audits in this case raise significant concerns about OVEC's operations that would be better assessed through a full hearing process. While several of the utilities agree to implement most of the auditors recommendations, they also attempt to misuse the prudence standard and rely on post-hoc rationalizations for imprudent and unreasonable costs. The OEC asks this Commission to deny all costs until it can complete a full hearing on this audit.

Respectfully Submitted,

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¹³ Initial Comments of Ohio Power Company in Response to the Audit Report, Case No. 21-0477, p. 7 (filed 5/8/2023).

CERTIFICATE OF SERVICE

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/s/Karin Nordstrom_____

Karin Nordstrom

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Summary: Comments Reply Comments In the Matter of the OVEC Generation
Purchase Rider Audits filed by Karin Nordstrom on behalf of the Ohio
Environmental Council electronically filed by Ms. Karin Nordstrom on behalf of Ohio
Environmental Council.