Consequences of First Energy's Electric Security Plan rehearing decision

December 5, 2016

On October 12, 2016, the Public Utilities Commission of Ohio (PUCO)approved the PUCO staff's proposal of a Distribution Modernization Rider (Rider DMR) in the First Energy Electric Security Plan (ESP IV) proceeding.[1] Thus, what began as an effort over two years ago by FirstEnergy to subsidize uncompetitive generation assets held by its affiliate, FirstEnergy Solutions (FES), turned into direct multi-year "credit support" payment of over $200 million to FirstEnergy from its captive ratepayers.

Although the decision will have immediate cost implications for FirstEnergy customers, there are other consequences of this decision.

Precedential implications of granting "credit support" payments?

Many intervening parties expressed concern that providing credit support payments to FirstEnergy would create a dangerous precedent, enabling other utilities to seek similar payments. In response, Chairman Haque stated that he is "not terribly concerned that we are setting dangerous precedent in this case by providing recovery based mathematically upon the financial condition of the utility."[2]

Whether the commission's decision creates precedent for future credit support payments will soon be put to the test. In a recent filing, the Dayton Power and Light Company (DP&L) requested approval of an annual Distribution Modernization Rider (DMR) in the amount of $145 million per year.[3] According to DP&L, "DMR is necessary to allow DP&L to access equity and debt capital in order to finance transmission and distribution infrastructure modernization investments."[4]

A focus on distribution assets instead of generation assets

The commission, by approving Rider DMR, determined that FirstEnergy should focus its resources on its regulated distributed systems, as opposed to a subsidy arrangement tied to its affiliate generation resources. PUCO found persuasive testimony arguing that "FirstEnergy should focus on the regulated side of the business and the competitive market—the distribution meters and wires."[5]

A. Implications for "re-regulation" efforts?

In response to Federal Energy Regulatory Commission's decision to block the affiliate support proposals approved in March 2016, American Electric Power (AEP) communicated that it intended to push Ohio's legislature to re-regulate power plants in Ohio.[6] Because FirstEnergy believes that the credit support provided by the commission through Rider DMR is not sufficient, it will likely be more inclined to push for legislative action to support its aging and uneconomic generation assets.

B. What does "grid modernization" mean?

To support its decision, the commission relied heavily on the concept of future grid modernization efforts.

The commission first determined that Rider DMR would provide a needed incentive for FirstEnergy to focus "innovation and resources on grid modernization."[7] It then determined that Rider DMR is authorized under R.C. 4928.143(B)(2)(h), which allows an ESP to include "provisions regarding distribution infrastructure and modernization incentives for the electric distribution utility."[8]

The potential downgrade of FirstEnergy's credit rating was viewed as a serious risk by the commission.[9] A downgrade, in PUCO's view, could lead to higher borrowing rates, increasing FirstEnergy's long-term cost of debt, leading to higher rates for customers, as well as its ability to invest in distribution infrastructure to maintain reliability or for investment in modernizing the grid.[10]

However, little detail was provided. Instead, the commission indicated that it "will undertake a detailed policy review of grid modernization in the near future."[11] Some clues may be found in FirstEnergy's "Grid Modernization Plan," filed in the FirstEnergy Grid Modernization Case.[12] This filing was a requirement in a settlement in the underlying ESP case. The grid modernization initiatives highlighted in the plan include advanced metering infrastructure, distribution automation, Integrated Volt/VAR Control, and distributed generation and net-metering tariffs.

Notably, the commission indicated that grid modernization efforts should extend beyond this plan.[13] Given the commission's expressed ambitions for grid modernization and "the future of the electricity industry," the intended future grid modernization proceedings could have significant implications for smart grid implementation, grid resiliency, battery storage technologies, electric vehicles and distributed generation.

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[1] Case No. 14-1297-EL-SSO.

[2] Id. at 4.

[3] *In the Matter of the Application of The Dayton Power and Light Company for Approval of Its Electric Security Plan*, Case No. 16-0395-EL-SSO, Amended Application (Oct. 11, 2016).

[4] Id. at 2.

[5] Entry at 50.

[6] See, "AEP pushing re-regulation after blocked profit guarantee," *Columbus Dispatch* (April 29, 2016), available at http://www.dispatch.com/content/stories/business/2016/04/29/1-FERC-folo.html.

[7] Id. at 88.

[8] Id. at 90.

[9] The Commission referenced a Moody's had issued a credit opinion on January 26, 2016, stating that certain factors could lead to a downgrade of FirstEnergy Corp.

[10] Id.

[11] Entry at 96.

[12] Case No. 16-0481-EL-UNC. It should be noted that AEP filed a similar plan.

[13] Entry at 89.

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