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September 25, 2013

Ms. Kirsten Walli
Ontario Energy Board
PO Box 2319
27th Floor, 2300 Yonge Street
Toronto, Ontario M4P 1E4

Re:     Consultation re: Measuring Performance of Electricity Distributors (EB-2010-0379)

Dear Ms. Walli,

On September 6, 2013, the Board released its "Draft Report of the Board on Empirical Research to
Support Incentive Rate-setting for Ontario's Electricity Distributors" (the "Draft Report").  A
consultation was subsequently held at the Board's office on September 11, 2013.

Entegrus Powerlines Inc. ("Entegrus") has been an active participant throughout this proceeding[1]
and appreciated the opportunity to attend this latest consultation.

At this time, Entegrus wishes to offer additional commentary and recommendations, organized
under the following sections by topic:

- Section 1:  The Productivity Factor
- Section 2:  The Stretch Factors & The Quintile Approach
- Section 3:  1998-2002 Capital Additions Data Issue

**Section 1:  The Productivity Factor**

Entegrus supports the determination in the Board's Draft Report that the productivity factor be set
at nil.  Entegrus notes that this determination is based on empirical study of distributor data by
expert consultants.

Dr. Kaufman (the PEG expert consultant) estimates the negative industry productivity experience to
be -0.3%.  Similarly, the EDA's expert consultant, Professor Adonis Yatchew, estimates negative
industry productivity of between -0.7% and -0.8%[2].  Mr. Steven Fenrick, expert consultant for the
Coalition of Large Distributors ("CLD"), summarizes the empirical findings as follows:

> *"… the 2002 through 2012 TFP has been measured to be negative.  All four experts appear to
> agree that over this time period it has been negative."*[3]

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[1] See Ontario Energy Board website / RRFE / Entegrus submissions dated:  June 27, 2013; June 24, 2013; May 31, 2013
[2] See Ontario Energy Board website / RRFE / Presentation of Professor Adonis Yatchew of  September 11, 2013:  page 3
[3] See Ontario Energy Board website / RRFE / Transcript of consultation of September 11, 2013:  page 67 ( lines 22-25)

While the data-based analysis shows a negative productivity factor, Entegrus supports the Board's determination to set the productivity factor at nil, rather than a negative value. Entegrus takes this view due to the undesirable implicit message to consumers and other stakeholders that would otherwise result.

Nonetheless, at the September 11 consultation, some participants advocated that the negative industry TFP trend should be studied in more detail[4], or alternatively that a "forensic TFP examination"[5] of IRM3 should be conducted. There was further discussion that indicated an additional six months might be required to facilitate such study.

Entegrus notes that the current consultation process commenced May 3 with the release of PEG's preliminary draft report. Since that time, there have been a total of four days of consultation and numerous commentary submissions from a cross-section of stakeholders, including extensive empirical analysis by the above-noted four expert consultants.

From a distributor perspective, the negative industry TFP trend is not a revelation. Rather, the trend is a function of industry change and numerous associated directives that distributors have responded to over the past 10 years. As noted by Professor Yatchew:

> *"Additional responsibilities undertaken by distributors as a result of the Green Energy Act, FIT programs, smart meters and other initiatives have also contributed to cost increases without increases in measured outputs."[6]*

In a follow-up report, Professor Yatchew further describes major Ontario policy and legislation changes that have affected the industry, notably those that have occurred over the period from 2002-2010.[7]

Accordingly, Entegrus submits that the drivers of the negative industry TFP trend are readily apparent and do not require further study. Entegrus believes that there has been sufficient time to dissect, discuss and corroborate the trend over the past five months of consultation. Additional study would come at the expense of "paralysis through analysis".

Entegrus asserts that it is critical to expedite the remainder of the empirical research phase of the RRFE process in order that price cap parameters are in place for 2014 distribution rates.

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[4] See Ontario Energy Board website / RRFE / Transcript of consultation of September 11, 2013: page 40 (lines 15-28), and page 41 (lines 1-12)
[5] See Ontario Energy Board website / RRFE / Transcript of consultation of September 11, 2013: page 122( lines 14-28), and page 123 (lines 1-9)
[6] See Ontario Energy Board website / RRFE / Presentation of Professor Adonis Yatchew of May 24, 2013: page 10
[7] See Ontario Energy Board website / RRFE / Electrical Distributor Association comments of June 27, 2013: pages 2-5

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**Section 2: The Stretch Factors & The Quintile Approach**

In its Draft Report, the Board has determined that distributors will be assigned to one of five cohorts, with different stretch factors for each cohort based on its efficiency as determined via PEG's econometric cost performance rankings.

PEG further describes the segmentation of the five cohorts as follows:

> *"Distributors whose actual costs are at least 20% below the costs predicted by PEG's cost model will be in the first cohort and assigned a stretch factor of zero. Distributors whose actual costs are between 15% and 20% below the costs predicted by PEG's cost model will be in the second cohort and assigned a stretch factor of 0.15%. Distributors whose actual costs are between 0 and 15% below the costs predicted by PEG's cost model will be in the third cohort and assigned a stretch factor of 0.3%. Distributors whose actual costs are between 0 and 15% above the costs predicted by PEG's cost model will be in the fourth cohort and assigned a stretch factor of 0.45%. Distributors whose actual costs are more than 15% above the costs predicted by PEG's cost model will be in the fifth cohort and assigned a stretch factor of 0.6%."[8]*

This non-symmetrical approach to cohort segmentation is shown in the updated PEG Report of September 6, 2013, as well as PEG's associated Excel file entitled "Tables in 2012 PEG Report". Entegrus has summarized the resultant distribution in Table 1 below:

**Table 1: Summary of PEG September 6, 2013 Tranche Distribution**

| Group | Scoring Range | Stretch | Distribution of Distributors | | |
|:-----:|:-------------:|:-------:|:----------------------------:|:---:|:-----------:|
| | (Actual Minus Predicted Cost) | Factor | # | % | Cumulative % |
| 1 | <= -0.20 | 0.00% | 5 | 7% | 7% |
| 2 | -0.20 to -0.15 | -0.15% | 7 | 10% | 17% |
| 3 | -0.15 to -0.00 | -0.30% | 18 | 24% | 41% |
| 4 | 0.00 to 0.15 | -0.45% | 26 | 36% | 77% |
| 5 | > 0.15 | -0.60% | 17 | 23% | 100% |

As shown above, the outcome of this scoring range distribution is that: 17% of distributors land into the top 2 cohorts, 41% of distributors land in the middle cohort and the remaining 59% of distributors fall into the bottom 2 cohorts. As noted by PEG, the result of this distribution is that, "*the average stretch factor for the industry will be [-] 0.37%*".[9] [10]

Entegrus cannot locate details in the report to show how these static scoring ranges were determined.

Entegrus submits that the distribution of distributors should be symmetrical, broken down into quintiles. Under this approach, the cohorts and the associated stretch factor distribution would be relative to other distributors. This would make the model less susceptible to data migration

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[8] See Ontario Energy Board website / RRFE / 2012 PEG Report of September 2013: pages 20-21
[9] Ibid: page 21
[10] **Note:** Entegrus believes that the resultant stretch factor based on this distribution actually calculates to -0.39%

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volatility that might otherwise occur over time due to the use of static scoring ranges, while still encouraging continuous improvement on a relative basis.

Further, the resultant relative cohort outcomes would be more understandable for stakeholders. Comparatively, explaining the meaning of cohort outcomes from a static scoring range perspective would be complex and confusing for stakeholders.

Entegrus acknowledges that the utilization of a quintile approach may appear to foment a competitive approach amongst distributors, akin to benchmarking. However, Entegrus feels that this is appropriate because the foundation of PEG's predictive econometric model is the data of other distributors. Accordingly, Entegrus views that this process is already inherently competitive, and thereby takes no issue with extending that approach to the segmentation of the cohorts.

Entegrus acknowledges that the proposed quintile approach would result in additional distributors moving into the top two tranches, since each tranche would have 14-15 distributors. In turn, this would equate to more distributors having lower stretch factors – the average IRM4 stretch factor would migrate to -0.30%. By comparison, the average 2013 stretch factor under IRM3 was -0.40%.

Customarily, stretch factors and productivity factors are considered in isolation. However, Entegrus notes that the determination to set the productivity factor at nil implicitly results in a stretch factor of between -0.3% to -0.8% (see Section 1 above). Accordingly, Entegrus submits that a decrease in the average stretch factor by 0.10% due to the adoption of a quintile approach would not be unreasonable.

**Section 3: 1998-2002 Capital Additions Data Issue**

On May 31, 2013, Entegrus submitted a letter of commentary to the Board noting the importance of using accurate historical capital data in PEG's total cost benchmarking calculations. Entegrus specifically raised concerns regarding the reasonability of certain capital asset addition figures determined by PEG though the use of estimation. A copy of this letter has been included as Attachment A.

On June 19, 2013, Entegrus received a response in this matter from PEG via Board Staff. PEG explained that two different estimate methods ("Method 1" or "Method 2") were applied on a case-by-case basis for each distributor in order to estimate figures for the period where industry capital additions data were not available. PEG further acknowledged that *"Entegrus was one company for which neither method generated highly plausible estimates of additions."* A copy of this response has been included as Attachment B.

In response, on June 24, 2013, Entegrus submitted a letter recommending that since the estimated data attributed to Entegrus was not plausible, another approach should be employed. Entegrus requested that the Board direct PEG to utilize a simple average of existing actual capital data to derive an estimate for Entegrus 1998-2002 capital asset additions as a means by which to more accurately represent historical capital additions. A copy of this letter has been included as Attachment C.

On September 6, 2013, the Board released the latest iteration of the 2012 PEG Report, along with

PEG's associated spreadsheet models.  In the spreadsheet entitled "TFP and BM Database Calculations 2012 WP", under the tab marked "Capital Calculations for BM" in cells T351 thru T355, the Entegrus 1998-2002 capital asset additions have been appropriately updated by PEG to values that closely approximate the figures recommended by Entegrus in its letter of June 24, 2013.  In cells U351 thru U353 of the same spreadsheet tab, there is an explanatory note, which indicates, *"Simple Linear Interpolation was used in place of Method 1 or Method 2"*.  Entegrus agrees with these adjustments and appreciates the assistance of the Board and PEG in this regard.

While the "Capital Calculations for BM" worksheet has been updated, this same adjustment to Entegrus 1998-2002 capital asset additions has not been flowed through to the "Capital Calculations for TFP" worksheet.  Specifically, in the same spreadsheet entitled "TFP and BM Database Calculations 2012 WP", under the tab marked "Capital Calculations for TFP" in cells V354 thru V358, the previous PEG "Method 2" is still being applied to derive Entegrus data.  This results in estimated capital additions for Entegrus for 1998-2002 of $9,406,434 annually.  As further described in Entegrus' previous correspondence (see Attachment C), this estimate is not plausible, given that Entegrus' actual 1997 additions were $3,740,567 and 2003 additions were $3,512,014.  When "simple linear interpolation" is applied in the same manner as described in the previous paragraph above, the capital additions become $3,626,291.  Entegrus believes this result to be more plausible, and consistent with the previous adjustment already made by PEG to the "Capital Calculations for BM" worksheet.  Further, it is the understanding of Entegrus that such an adjustment would affect the econometric model's "actual versus predicted costs" outcome for Entegrus.

Accordingly, Entegrus respectfully requests that the Board direct PEG to update the tab marked "Capital Calculations for TFP" in cells V354 thru V358 to reflect capital additions of $3,626,291, and consequently update the model results.

If you have any questions, please do not hesitate to contact me.

All of which is respectfully submitted,

*[Original Signed By]*

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