Barristers & Solicitors

WeirFoulds LLP

July 8, 2009

Robert B. Warren
T: 416-947-5075
rwarren@weirfoulds.com

Kirsten Walli
Board Secretary
Ontario Energy Board
Suite 2701
2300 Yonge Street
Toronto ON M4P 1E4

Dear Ms Walli:

Re: The Regulatory Treatment of Infrastructure Investment for Ontario's Electricity Transmitters and Distributors – EB-2009-0152

On June 10, 2009, the Ontario Energy Board ("Board") initiated a consultation process with stakeholders to consider more innovative approaches to cost recovery for electricity infrastructure projects. Board Staff prepared a paper entitled, "Staff Discussion Paper on The Regulatory Treatment of Infrastructure Investment for Ontario's Electricity Transmitters and Distributors." ("Staff Paper") The Staff Paper is intended to solicit input from all interested stakeholders on a range of alternative mechanisms within an integrated framework for the regulatory treatment of infrastructure investment. The Board is seeking comments on the paper. These are the comments of the Consumers Council of Canada ("Council").

Overview:

On April 3, 2009, the Board Chair issued a statement to all interested stakeholders indicating the Board's intent to examine alternatives to its current approach to cost recovery from ratepayers for capital investment. On May 14, 2009, the *Green Energy and Green Economy Act, 2009* ("GEA") was given royal assent. The GEA establishes the connection of renewable energy generation facilities and the development of a "smart grid" as policy priorities for the Government. In addition, the GEA adds as objectives for the Board, the promotion or facilitation of renewable energy and smart grid investments. There is an expectation in Ontario that significant capital spending will be required by distributors and transmitters to facilitate these two new policy goals. In initiating this review the Board is assuming that the existing regulatory framework is not sufficient to accommodate that new investment.

The Council recognizes that the GEA will bring forward significant changes to the electricity sector in Ontario. Increased reliance on renewable energy potentially changes the way in which transmitters and distributors operate their systems. The emergence of a smart grid will require new technologies and related investments. Ramping up conservation activities will come with both costs and benefits. The Board must consider how all of these activities will impact rates for end-use customers. There is no reason to think that the current regulatory framework and the rate-making mechanisms available within that framework are not sufficient to balance the interests of the ratepayers and the utility shareholders. On the contrary, since one of the principal objectives of the existing regulatory framework is the protection of consumers, the operating assumption should be that that framework should not be changed.

Board Staff has noted that electricity rate-regulated companies, particularly distributors and transmitters are currently investing substantial amounts of capital to replace aging infrastructure, deploy smart meters, to connect new load and maintain system operability and reliability (Staff Paper, p. 5). These investments have been taking place over the past several years and have been the subject of numerous rate proceedings. To date existing mechanisms have proven sufficient to allow Ontario transmitters and distributors make the capital investments that have been required. It is not at all clear why "infrastructure investments" arising out of the new objectives and requirements of the GEA warrant movement away from traditional utility rate-making principles.

In putting forward alternative rate-making mechanisms for consideration Board Staff has relied heavily on two U.S. publications. The first is the Federal Energy Regulatory Commission's ("FERC") July 20 Final Rule Promoting Transmission Investment through Pricing Reform. The second is a paper written by Scott Hempling and Scott H. Strauss entitled, *Pre-Approval Commitments: When and Under What Conditions Should Regulators Commit Ratepayer*

Ratepayer Dollars to Utility Proposed Capital Projects? issued in November 2008. Board Staff has noted that:

> these two documents reflect a thoughtful analysis of the issues and concerns relating to new and more challenging infrastructure needs, as well as of the potential approaches to dealing with those issues and concerns. While staff recognizes the need to ensure that solutions adapted from other jurisdictions are suited to the Ontario context, staff believes that these documents provide a sound basis for developing a similar approach in this Province. (Staff Paper, p. 3)

The context in which these papers were developed and the current environment in Ontario are not the same. The mechanisms addressed in those papers were undertaken when FERC was looking to create incentives for investor-owned utilities to invest in aging infrastructure. Hydro One Networks Inc. ("HON"), in its 2007/2008 transmission rate application, applied for approval of an alternative regulatory accounting treatment for several of its large capital projects. HON relied on the FERC practice, but its submissions were rejected by the Board as not applicable to the Ontario context. (Decision with Reasons, EB-2006-0501, pp. 60-63) In Ontario, distributors and transmitters are being directed to file plans to accommodate renewable generation and/or the development of the smart grid. On June 16, 2009, the Board issued guidelines related to the accounting, funding and planning for distributors to follow in developing these plans. In addition, many provisions in the GEA and related codes and regulations mandate expedient connection of renewable generation, under terms and conditions that are much more flexible than those in the past. The need to create "incentives" for investments arising out the GEA is neither required nor necessary.

The GEA provides for a mechanism by which Board-approved costs incurred by a distributor to make an "eligible investment" for the purpose of connecting or enabling the connection of a "qualifying generation facility" to its distribution system may be recovered through contributions payable by all consumers in the Province. (section 79.1 GEA). In effect, distributors and or transmitters, may have some or all of the costs related to investments made pursuant to the

GEA funded by customers across the Province. It is not at all clear how the Government and/or the Board intends to use this mechanism. Until that becomes clear, it would be premature to move away from traditional rate-making mechanisms. If transmitters and distributors were able to fund investments through a Province-wide fund, why would there be a need to introduce additional alternative approaches to cost recovery?

<u>Conclusions:</u>

The Council submits that the discussion set out in the Staff Paper does not warrant the movement in Ontario to new regulatory framework for distribution and transmission infrastructure investment. The Council supports the continued use of existing cost recovery mechanisms, consistent with long-standing regulatory practice. For the reasons set out below the Council believes the Board has sufficient tools in place to ensure recovery of prudent capital investment and it would be premature, if not unnecessary to move away from a framework that has proven fair to both ratepayers and utility shareholders:

1. Board Staff has not demonstrated why the existing regulatory framework and cost recovery mechanisms are not adequate, and why in particular, they are not adequate for new infrastructure investments arising out of the GEA. Traditional cost of service rate-making has always allowed for the recovery of prudent capital expenditures. The Incremental Capital Module component of the 3rd Generation Incentive Regulation Mechanism, allows distributors to seek rate relief to the extent unusual circumstances arise during the term of an IRM plan. Deferral accounts and Z-factors also accommodate the recovery of expenditures that are not necessarily routine. Rate riders allow for recovery over various time frames. Currently the Board allows for interest to accrue during construction of a project and, once the assets are used and useful, the costs including the interest are transferred into ratebase;

2. Board Staff has relied on mechanisms developed in the U.S., in an entirely different context. There is no evidence that Ontario distributors and transmitters, the majority of which are publicly owned, need incentives to invest in projects that are effectively mandated by the GEA;

3. Board Staff has not established why there should be a distinction between the regulatory investments made pursuant to the GEA and other capital projects;

4. There is no clarity yet regarding how, and to what extent, expenditures related to renewable power and a smart grid will be recovered on a Province-wide basis. Until that clarity is obtained, it would be premature to establish a new menu of rate recovery mechanisms.

5. The Board must continue to set just and reasonable rates and meets its mandated objective to protect the interests of consumers with respect to prices. The current framework does this. It is not clear, under the proposed alternative mechanisms, the extent to which the Board's obligation would be compromised by introducing mechanisms that could shift the risk of certain investments unfairly onto utility ratepayers.

6. It is important that any expenditure for which a utility seeks approval should continue to be subject to an economic feasibility test. In the absence of such a test, comprehensive evidence as to why the expenditure is justified should continue to be a requirement;

7. The Staff Paper suggests that adopting a case-by-case approach to the review and approval of applications, for one or more alternative mechanisms, to encourage appropriate investment may provide the most effective way of balancing the unique challenges and the particular circumstances of an applicant with the public interest (Staff Paper, p. 15). This could potentially result in an ad hoc regulatory framework in the Province with certain utilities subject to all sorts of different accounting treatment for

similar investments. It may also result in different accounting treatment for similar assets within one utility. This will only add to what is already a complex regulatory construct.

The Council recognizes that Ontario distributors and transmitters can always bring forward proposals for their rates to be set on an alternative basis. HON brought forward a proposal, in the context of its 2007/2008 transmission rates proceeding, for a unique accounting treatment applicable to a certain set of assets that was considered by the Board, and ultimately rejected. The Council submits that this is very different than the Board establishing, and promoting, a new framework, whereby a menu of alternative cost recovery mechanisms would be available. For the reasons set out above the Council does not support the establishment of such a framework. The passage of the GEA does not justify an abandonment of established regulatory principles and rate-making mechanisms. There has been no evidence provided to demonstrate that the objectives of GEA cannot be adequately facilitated under the current framework.

The only reason to adopt new regulatory mechanisms would be to reduce, if not eliminate, public scrutiny of significant investment proposals. That would be contrary to the Board's obligation to protect the interests of consumers.

To the extent the Board is of the view that it intends to promote a new framework, and allow for alternative rate-making mechanisms, the Council supports the case-by-case approach. The evidentiary burden should be significant, and the utilities required to clearly demonstrate that they cannot meet the requirements imposed upon them by the GEA under the current regulatory construct. The expectation should be that approval of alternative approaches to deal with infrastructure costs would be the exception and not the norm.

The Council urges the Board to give careful consideration of these issues and the potential impacts they may have on ratepayers. Ontario electricity ratepayers are facing continued increases with respect to all elements of the bill - distribution, transmission and commodity costs. These rate impacts will only increase if the Board makes decision that shifts the risk of implementing the GEA unfairly on utility ratepayers.

The Council looks forward to its ongoing participation in this consultation process.

Yours very truly,

WeirFoulds LLP

Robert B. Warren

RBW/dh

c: Joan Huzar, Consumers Council of Canada
c: Julie Girvan

1133164.1