

**SUBMISSIONS OF ST. THOMAS ENERGY INC.  
IN RESPECT OF NOTICE OF PROPOSAL TO AMEND A CODE:  
PROPOSED AMENDMENTS TO AFFILIATE RELATIONSHIPS CODE FOR  
ELECTRICITY DISTRIBUTORS AND TRANSMITTERS**

**I. INTRODUCTION**

These are the submissions of St. Thomas Energy Inc. ("STE") in respect of Ontario Energy Board's (the "Board") Notice of Proposal (the "Notice") to amend the Affiliate Relationships Code for Electricity Distributors and Transmitters (the "ARC").

STE acknowledges the efforts of the Board in preparing the Notice and welcomes the opportunity to provide its comments. However, as STE stressed in its July 23, 2007 submission in this proceeding, the process of review and comment undertaken in this proceeding should not replace the need for a full review of the ARC and amendment process as provided for in Section 70.2 of the *Ontario Energy Board Act, 1998*, (the "OEB Act"). In STE's view, the Board should embark on a code review similar to that undertaken by the Board in respect of the Transmission System Code in order to resolve many of the issues raised and to eliminate the uncertainty relating to the interpretation of the ARC.

**II. ECONOMIC EFFICIENCY AND COST EFFECTIVENESS**

The OEB Act specifically states that one of the two objectives of the Board is to promote economic efficiency and cost effectiveness in the distribution sector. This purpose is further reinforced under the purposes of the *Electricity Act, 1998*.

In the Notice, the Board indicated that it has excluded the objective of promoting economic efficiency and cost effectiveness in the distribution of electricity from the ARC (at page 5):

"The Board does not believe that the addition of a reference to utility efficiency or cost effectiveness as an objective of the Electricity ARC is necessary. Promoting economic efficiency and cost effectiveness in the distribution and transmission sectors is a statutory objective of the Board, but it is not the primary purpose or objective of the Electricity ARC."

The promotion of economic efficiency and cost effectiveness in the distribution sector is a statutory objective of the Board that must adhere to in all respects, including the regulation of

relationships between electricity distributors and their affiliates. A number of affiliate relationships exist for the purpose of maximizing the economic efficiency and cost effectiveness in accordance with paragraphs 5 and 6 of subsection 73(1) of the OEB Act:

"If one or more municipal corporations owned, directly or indirectly, voting securities carrying more than 50% of the voting rights attached to all voting securities of a corporation that is a distributor, the distributor's affiliates shall not carry on any business activity other than the following:

1. Transmitting or distributing electricity.
2. Owning or operating a generation facility that was transferred to the distributor pursuant to Part XI of the *Electricity Act, 1998* or for which the approval of the Board was obtained under Section 82 or for which the Board did not issue a notice of review in accordance with Section 80.
3. Retailing electricity.
4. Distributing or retailing gas or any other energy product which is carried through pipes or wires to the user.
5. **Business activities that develop or enhance the ability of the distributor or any of its affiliates to carry on any of the activities described in paragraphs 1, 3 or 4.**
6. **Business activities the principal purpose of which is to use more effectively the assets of the distributor or an affiliate of the distributor, including providing meter installation and reading services, providing billing services and carrying on activities authorized under Section 42 of the *Electricity Act, 1998*.**
7. Managing or operating, on behalf of a municipal corporation which owns shares in the distributor, the provision of a public utility as defined in Section 1 of the *Public Utilities Act* or Sewage Services.
8. Renting or selling hot water heaters.
9. Providing services related to the promotion of energy conservation, energy efficiency, load management or the use of cleaner energy sources, including alternative and renewable energy sources." (Emphasis added)

Because the promotion of economic efficiency and cost effectiveness in the distribution and transmission sectors is a legislative objective of the Board, and is the basis of affiliate relationships in accordance with subsection 73(1), STE submits that it is imperative that the ARC specifically include that objective in the ARC as a primary objective or, at the very least, as one of the ARC's objectives. Deliberately excluding this objective from the ARC implies that the

Board does not consider the promotion of economic efficiency and cost effectiveness in the distribution and transmission sectors to be a relevant consideration in regulating the relationship between distributors and their affiliates, *ultra vires* the statutory objectives set out in the OEB Act.

Although the Board has stated in the Notice that it takes account of utility efficiency and cost effectiveness concerns when determining to make the provisions more or less restrictive, the objective of promoting economic efficiency and cost effectiveness may be lost in future interpretations and applications of the ARC if it is not specifically included in the ARC.

### III. TRANSFER PRICING

STE submits that the transfer pricing provisions in the ARC should in no way limit utilities from outsourcing their OM&A requirement to one affiliated supplier. To do so could significantly impair economic efficiency and cost effectiveness.

One could argue that outsourcing OM&A requirements to one supplier amounts to “bundling” of services (STE expressly disagrees with the argument). At page 11 of the Notice, the Board endorses Compliance Bulletin 200604 in regard to determining whether a competitive market exists:

“...a utility must of necessity conduct a market review to determine whether reasonably a competitive market exists, as described in Compliance Bulletin 200604...”

Compliance Bulletin 200604 suggests that a review to determine whether a competitive market exists for bundled services is unacceptable (i.e. the determination of a competitive market must be made on a service-by-service basis):

“Bundling a number of distribution services together so that they form a unique service requirement that cannot be provided by any entity other than the affiliate cannot, in my view, be used as a means of eliminating the possibility of a market existing for specific services.”

STE submits that the potential for interpreting outsourcing OM&A to one affiliated supplier as “bundling”, and the Board’s endorsement of Compliance Bulletin 200604 could effectively limit a distributor’s ability to outsource OM&A to one affiliated supplier. If this were to occur,

economic efficiency and cost effectiveness could be jeopardized, since significant cost savings can be realized by outsourcing OM&A to one affiliate (i.e. increased bargaining power and economies of scale). Accordingly, STE requests that the Board acknowledge that the outsourcing of OM&A to one affiliated supplier does not amount to “bundling”.

#### **IV. STRATEGIC BUSINESS INFORMATION**

The Board has proposed that the ARC include a new provision that restricts a distributor from providing strategic business information to an affiliate that is an energy service provider:

2.6.4 A utility shall not provide strategic business information to an affiliate that is an energy service provider.

“Strategic business information” is defined as

“strategic business information” means information, including confidential information, that a utility has obtained or developed in the course of providing, or otherwise has in its possession as a result or for the purpose of providing, current or prospective utility service and that (a) identifies or can reasonably be expected to identify or (b) provides or can reasonably be expected to provide a business opportunity or other business advantage to the person to whom the information is provided;”

STE submits that these provisions create a restriction that is ambiguous and will be difficult, if not impossible, for distributors to self-monitor. For example, it is unclear what information the Board believes will provide a “business opportunity” or “business advantage”. Further, it is not clear how the Board interprets “business opportunity” or “business advantage”. Unless the Board can succinctly describe distributors’ obligations in regard to strategic business information, STE submits that the section will serve as the source of confusion and should therefore not be included in the ARC.

Further, section 2.6.4 is problematic from a corporate governance perspective. It is not uncommon for distributors’ officers and directors (who do not have access to confidential information as defined by the ARC) to hold equivalent positions with affiliates. This is common practice in the industry and is even acknowledged by the Board:

- section 2.1.3 of the ARC allows for common directors between distributors and their affiliates, subject to 1/3 independence; and
- section 2.3.5.1 in the Notice addresses “shared corporate services”, which are defined in the Notice as “business functions that provide shared strategic management and policy support...”.

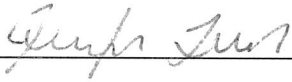
A distributor’s officers and directors must be kept apprised of and consider strategic business information related to the distributor. They would also be aware of that information in their capacity as officers and directors of the affiliate. Therefore, section 2.6.4 would restrict officers and directors from having dual roles with distributors and affiliates. Such a restriction pose significant corporate governance challenges for distributors and would contradict section 2.1.3 of the existing ARC and section 2.3.5.1 contained in the Notice.

## V. CONCLUSION

1. *Economic Efficiency and Cost Effectiveness:* It is imperative that the ARC specifically include the objective of the “promoting economic efficiency and cost effectiveness in the distribution and transmission sectors” as a primary objective or, at the very least, as one of the ARC’s objectives. Deliberately excluding this objective from the ARC implies that the Board does not consider this objective to be a relevant consideration in regulating the relationship between distributors and their affiliates, *ultra vires* of the objectives set out in the OEB Act.
2. *Transfer Pricing:* The potential interpretation that outsourcing OM&A to one affiliated supplier amounts to “bundling”, and the Board’s endorsement of Compliance Bulletin 200604 creates a scenario that could jeopardize economic efficiency and cost effectiveness. Accordingly, STE requests that the Board acknowledge that outsourcing OM&A to one supplier does not amount to “bundling”.
3. *Strategic Business Information:* The proposed restriction is ambiguous and will be difficult, if not impossible, for distributors to self-monitor. Unless the Board can succinctly describe distributors’ obligations in regard to strategic business information, STE submits that the section should not be included in the ARC. As well, the proposed

restriction poses significant corporate governance challenges for distributors and would contradict section 2.1.3 of the existing ARC and section 2.3.5.1 contained in the Notice.

All of which is respectfully submitted by



PU

Charles Keizer, Solicitor for St. Thomas Energy Inc.