

Norton Rose Canada LLP
TD Waterhouse Tower, Suite 2300
Toronto-Dominion Centre
79 Wellington Street West, P.O. Box 128
Toronto, Ontario M5K 1H1 CANADA

F: +1 416.360.8277
nortonrose.com

On January 1, 2012, Macleod Dixon joined
Norton Rose OR to create Norton Rose Canada.

Direct line
+1 416.202.6741

April 20, 2012

Via Courier and RESS

Ms. Kirsten Walli
Ontario Energy Board
Box 2319
2300 Yonge Street
Suite 2700
Toronto ON M4P 1E4

Our reference
280138

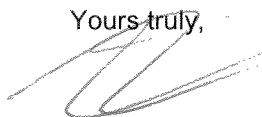
Email
robert.frank@nortonrose.com

Dear Ms. Walli:

**Written Comments on Behalf of the Electrical Contractors Association of Ontario,
Renewed Regulatory Framework for Electricity: EB-2010-0377 and EB-2010-0379**

Further to the Ontario Energy Board's letter dated April 5, 2012, enclosed are the written comments filed on behalf of the Electrical Contractors Association of Ontario in respect of the above matter.

Yours truly,



Robert Frank
RIF/ss

Enclosure

Copy to: Eryl Roberts, Electrical Contractors Association of Ontario (via email)

Written Comments of the Electrical Contractors Association of Ontario

Renewed Regulatory Framework for Electricity EB-2010-0377 and EB-2010-0379 April 20, 2012

Electrical Contractors Association of Ontario

ECAO is a not-for-profit corporation established to represent electrical contractors across Ontario. ECAO has 850 member contractors that provide a broad range of electrical services in the institutional, commercial, industrial, residential and electrical utility, construction and maintenance marketplace. ECAO members have done extensive work constructing connection facilities for Ontario's privately-developed electricity generation facilities, and certain capital construction work for regulated entities. Its members and their customers are directly affected by, and interested in, the regulation of network investment plans by transmitters and distributors.

One of ECAO's central objectives is to increase electricity customer efficiency, choice and access to electricity services through competitive services, and to provide cost-effective contracting services for capital construction by regulated entities.

Regulate to incentivize lower capital costs

In addition to pacing and prioritization of planning, the renewed regulatory framework for electricity distributors and transmitters (RRFE) should measure and incentivize cost avoidance. One method of avoiding costs is by incentivizing conservation methods which can decrease consumption and, therefore, the cost of electricity. Another method is to put in place incentives which lead to lower capital construction costs.

The current regulatory model does not evaluate the economic efficiency of capital construction, nor does it incentivize behaviour which leads to lower capital costs of construction (i.e. cost avoidance). The RRFE must do so. A simple and effective manner to lower the cost of capital construction, and therefore lower rates, is to include an evaluation of capital construction input costs as part of a rate-setting process. To do so, the renewed regulatory model must assess whether capital construction is being procured at competitive market prices. This should apply to all types of investments: connection assets, expansions, enhancements, and renewable enabling improvements.

In-house capital construction is pervasive and inefficient

There is a hugely disproportionate amount of capital construction in Ontario that is performed in-house. This occurs because project input costs are not evaluated against competitive market prices, and because the current regulatory scheme in Ontario does not properly incent economically efficient behaviour in respect of capital construction. In-house performance of capital work is generally not cost-effective. It is often performed inefficiently and at inflated costs, which comes at a substantial financial cost to Ontario's ratepayers and fosters other inefficiencies.

The typical procurement processes for Ontario's regulated entities must be compared to those employed by transmitters and distributors in provinces such as Alberta, British Columbia, New Brunswick and Nova Scotia. In those provinces, contracting out of capital construction projects is much more commonplace thereby enhancing the ability of industry participants to deliver timely services, particularly in times when significant capital investment is required. In Ontario, there should no longer be a presumption that the use of an in-house workforce for capital construction is appropriate or efficient. Regulated utilities should be required to demonstrate the efficiencies gained by an in-house workforce employed to perform capital construction work.

Incentivize competitive, market-based procurement

The RRFE must incentivize competitive, market-based procurement processes. This would lead to efficiencies in the Ontario electrical contracting industry in terms of the cost and timeliness for delivery of capital construction services. These efficiencies are particularly important at times when there is a need in the province for significant capital investment, such as in the current environment.

In the renewed regulatory framework, proper incentives should be put in place to ensure that appropriate performance metrics are used to assess the effectiveness of managing capital construction costs. Productivity and cost efficiency benchmarks and other evaluation mechanisms should be used to serve this purpose. In all cases, capital construction costs should be assessed for value.

Where services are contracted out, they should be procured using a competitive model such as public tendering. Where they are not contracted out, there should no longer be a presumption that the choice was appropriate. Rather, where performed in-house or through affiliates, regulated entities should be required to demonstrate the economic efficiency of project costs, and the capital construction costs must be assessed for reasonableness against competitive market prices.

Evaluation mechanisms

While the choice of evaluation mechanisms is not without its challenges, it is clear that metrics are needed to assess capital construction costs against competitive market costs. Assessment should include an outcomes-based approach as well as an *ex post* analysis.

Appropriate evaluation mechanisms in respect of capital spending can include benchmarking. Benchmarking of capital spending could be based on past performance, peer performance or sector performance. Ideally, Ontario data would be applied, where available.

Evaluation can also include prudence reviews, which should evaluate whether regulated entities are employing best practices. In the context of capital costs, this should include an assessment of the following types of factors:

- are the procurement processes reflective of the competitive marketplace?
- are administration costs controlled such that they are consistent with those found in private markets?
- how accurately are costs being measured?
- how efficient is the use and tracking of equipment and inventory related to project construction?
- are appropriate safety and quality construction standards being met?

Long-term investment planning

Long-term investment planning will allow industry participants to understand the anticipated needs for capital construction and make informed decisions about investment in plant, equipment and personnel. It is recognized, however, that there are certain challenges associated with long-term investment planning in terms of cost benchmarking for capital construction costs.

Conclusion

Incenting efficiency of capital construction costs serves all ratepayers well, and must be a necessary part of the RRFE. However, the current regulatory model does not assess the capital construction procurement processes of regulated entities for economic efficiency, nor does it incentivize behaviour which will avoid costs. Rather, the current model fosters in-house performance of capital construction

which is not being assessed against market pricing, and which comes at a real economic cost to ratepayers.

Competitive procurement processes decrease costs and ensure efficiency of the contracting industry. Under the RRFE, the procurement processes of regulated entities must be evaluated for economic efficiency. Going-forward, it must no longer be presumed that the in-house performance of capital construction work is economically efficient. A combined outcomes-based approach with benchmarks and *ex post* analysis is appropriate and necessary to achieve economic efficiency in respect of capital construction costs.

ECAO appreciates the opportunity to present its views, and looks forward to the opportunity to continue as an active and responsible participant in the RRFE initiative.