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Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
PO Box 2319
2200 Yonge St
Toronto, ON M4P 1E4

Dear Ms. Walli:

Subject: Renewed Regulatory Framework for Electricity

We welcome the opportunity of submitting our views and suggestions for consideration in connection with your interest in improving Ontario's regulatory framework for electricity. This is a very worthwhile and timely initiative which we believe should have as its overarching objective improving the cost effectiveness of regulation for the benefit of electricity consumers.

Guelph Hydro is a member of the Electricity Distributors Association ("EDA") and of the mid-size LDC group ("MSDG"). In addition to the submissions being made by these organizations, Guelph Hydro suggests the following for the OEB's focus:

- migrate the structure of LDC rates to better reflect the fact that most costs are independent of the volume of electricity consumed.
- for individual customers that represent more than 5% of an LDC's gross revenue, reduce the liability of the LDC to collect on behalf of others in the wholesale supply chain by allocating liability throughout the supply chain in proportion to revenue share from that customer.
- reduce regulatory costs by advancing more aggressively with the IRM initiative and specifically by forbearing from a formal regulatory review of any LDC that meets pre-determined metrics with regard to O&M costs, ROE and long-term planning.
- reduce the frequency and detail of required routine reporting to be consistent with the above improved IRM structure.
- review the ARC in light of experience since it was first implemented and with a view to focusing on the protection of customer interests by preventing cross-subsidization and providing cost-effective services rather than artificially creating competitive opportunities for third parties.
- work with LDCs to build customer confidence and understanding by simplifying the billing format and communicating regulatory decisions in more easily understood language and format.
- be consistent with the broader initiatives to streamline regulation, restrict intervenors to those who have a direct customer involvement in the LDC's service area.

The balance of this letter elaborates these points in turn.

Fixed and Volumetric Costs

Consideration might be given to migrating the rate structure for the LDC component of customer bills such that a higher proportion of revenues are recovered through fixed charges and a correspondingly smaller portion is dependent on the volume of consumption. Most of the costs incurred by an LDC for providing services do not materially change with changes in consumption and such a change would therefore more accurately reflect cost causality. Under the current structure, rates are based on a forecasted assumption of volume however small, forecasting error is inevitable and introduces elements of risk, cost and complexity.

While consumption-based pricing is of course important to encouraging the efficient use of our energy resources, the issue of fundamental importance is that customers see pricing that reflects cost structure so that as changes related to such things as microFIT projects, electric vehicles and smart grid occur over time, the rate changes they trigger continue to be fair and predictable.

Large elements of the cost of electricity service relate to the cost of the delivery infrastructure and not the electricity itself. Such costs are more accurately reflected in a fixed charge related to having a connection to the system rather than to the volume of electricity that flows over that connection. It will be beneficial for customers to have a greater awareness of this as, for example, rooftop solar and plugin hybrid or electric cars become more prevalent and blur the distinction between grid supply and non-grid supply. The cost of a backup grid connection for customer-owned generation and storage devices will be very difficult to recover equitably with the current rate structure which is dominated by volume-dependent rates.

We recognize that some customers may not welcome such a change as they are used to thinking about the level of demand they put on the system as being indicative of their fair share of the costs. For that reason, we suggest that this be an initiative taken progressively over some time. As well, it deserves to be preceded by OEB direct engagement with customers themselves both to explore attitudes and stimulate thinking, but the bottom line, if adopted will undoubtedly impact the cost of regulation positively.

Credit Risk Allocation

Guelph Hydro recommends changes to the credit risk allocation between an LDC and the IESO, OEFC, various generators and Hydro One. The intention of this proposal is to ensure that credit risk is allocated in proportion to the benefit received. At present, an LDC is required to make payments to entities like IESO, OEFC, various generators and Hydro One regardless of whether the LDC itself was paid by the customer. In effect, the LDC becomes the 100% guarantor of its customer when the LDC receives only approximately 20% of the customer's payment. The associated risk accrues directly to the LDC's cost of capital which, in turn, skews the apparent cost benefit ratios of LDC and bulk supply investments. With new investments required to support smart grid and distributed generation, customers will benefit from ensuring that investment costs across the system are reflected accurately and that local investments are not disadvantaged. This will be achieved by allocating the credit risk throughout the supply chain in proportion to the revenues each entity receives, rather than being borne entirely at the distribution level.

The risks under the current model are made more significant by the common practice in bankruptcy situations of the courts ordering the continuation of electricity service. While there are clearly circumstances where it is in the public interest to continue providing service it is not appropriate to burden LDC ratepayers with costs for doing so beyond those associated with the revenue they have been receiving for local investment and operating costs. We suggest consideration be given to an arrangement that if a customer representing 5% or more of a distributor's revenue becomes unable or unwilling to pay its bill, the distributor should have a mechanism to proportionally decrease the amount it owes other entities in the supply chain. By doing so, all entities in the supply chain will proportionally share in the credit risk currently borne by a distributor alone.

Regulatory Cost Effectiveness

Guelph Hydro recently prepared and submitted over 4,000 pages of evidence to the OEB as part of its rate rebasing proceeding. This effort required significant resources including many hours of senior employees' time. There is an opportunity cost associated with this effort, as, instead of completing other tasks, Guelph Hydro's limited resources were devoted to the preparation of these documents. While there may be special circumstances that may justify this massive effort, a cost effective regulatory system should not require it routinely and frequently.

We believe that the Incentive Regulatory Mechanism (IRM) that the OEB has pioneered in Ontario be enhanced and further developed to capture savings from reducing regulatory overhead. For example, if a distributor meets these three criteria, the OEB could forebear from engaging in the time consuming and costly process of rate re-basing: 1) the operations and maintenance and administration ("OM&A") constraint; 2) the return on equity ("ROE") constraint and 3) an approved long term (no more than 10 year) capital or asset management plan and of course, all balanced against the rate of inflation.

The OM&A constraint would be designed to limit annual spending increases within a band or range determined by the OEB (e.g., from 0 to 3%), again tested against inflation. If an increase falls within the band, there would be no need for detailed OEB review, the cost of which would rival the size of any savings customers might see. This would not only provide strong discipline to OM&A spending but it would also discourage year-end spending surges by removing the fear that in the following year the ability to have any increase in spending would be gone.

Similarly, the ROE constraint would create an incentive for the LDC to spend and invest capital within the range determined by the OEB. An LDC that spends too little would earn an excess return, which it would have to repay to its rate payers, while one that spends too much would receive a lower return, and would have to reduce its dividend to its shareholder. These two constraints, working together, would create the incentive for LDCs to invest the "right" amount in capital replacement and upgrading each year, to avoid necessary investments being foregone and simply passed on to the next generation of rate payers.

Assuming that an LDC's proposed spending increases fall within the two constraints listed above, and are consistent with its long-term capital plan, customers interests will be better served by avoiding the costs of an in-depth review by OEB.

The ranges set by the OEB for both OM&A and ROE would be informed by a long-term plan (for example, no more than 10 years) which each LDC should be required to submit. These plans should be updated annually and therefore would be a rolling plan that balances both the stability of a long look forward with the adaptability for shorter term and unexpected changes in externalities.

Within this structure, the OEB would have the ability to "call in" an LDC for a rebasing review. This might occur, for example, no more than every 10 years, or if the rate of return exceeds the allowed rate of return by 1 percentage point or more. As well, the LDC would be free to apply for a rebasing if it faces unexpected costs or demands on its resources. Again, the objective is to ensure that formal regulatory hearings occur only when their costs are outweighed by their benefits to customers.

Reporting
Similarly, the cost effectiveness of current routine reporting requirements should be reviewed. For example, Guelph Hydro is now required to prepare 23 reports monthly, plus 5 quarterly reports, plus 14 annual reports. This creates costs both at the LDC level and, we presume, at the OEB. Consideration should be given to the value which accrues to customers and its relationship to these costs. It seems reasonable that reporting should cover the core issues affecting the industry, namely, the reliability of the LDC, the allowed ROE, the administrative expense as a percentage of total operating costs, and the LDC's capital programs. Beyond this, it is unclear what value is derived from, for example:

- OEB Report 2.1.15 - Generator Connection (Quarterly)
- Smart Meter/Time of Use Reporting (Monthly)

The Affiliate Relationship Code ("ARC")
A strict, literal interpretation of the ARC leads to inefficiencies and increased costs. The ARC is also, in some respects, outdated, and its repeal should be seriously considered. Today, the ARC is largely symbolic and impractical in its application. The ARC is designed to protect against sharing of customer information between regulated and unregulated affiliates, and to ensure that the regulated entity does not give its unregulated affiliate any competitively unfair advantage. These are worthy objectives, but not the only worthy objectives to be considered, and therefore, should be balanced against other worthy objectives. From a customer's perspective, protection against cross-subsidies from regulated to unregulated activities and ensuring lowest cost provision of services are the most important considerations. After all, competition is not an end in itself but rather it is customers' expectation of cost effective services that provides the rationale for facilitating competition.

If the ARC is interpreted literally, it forces a regulated LDC to incur additional costs to provide services for which there may be little or no competition because other, unrelated parties are not interested in providing them. Customers will be better served if competitive services are facilitated only where such competition actually exists, or has a realistic chance of emerging in the near future. Otherwise, the ARC adds needless costs by erecting barriers to the cost effective provision of services.

For example, Guelph Hydro uses its service crews to repair streetlights when its service crews have availability or down time. Given the significant role electricity line crews have in local and provincial emergency response arrangements, staffing levels inherently provide capacity to take on such work at low marginal costs. By doing so, Guelph Hydro increases its efficiency and smoothes the workload for its service crews. However, the ARC requires Guelph Hydro to allow a third party to bid for its streetlight maintenance work against the LDC. In Guelph, no one else has expressed any interest that we are aware of, in bidding for this business. Even if there were an unrelated entity interested in bidding, it likely could not provide the service at as low a cost, which probably accounts in part for the lack of interest. Awarding an unrelated entity the contract could therefore increase streetlight servicing costs for the consumer of this service, the City of Guelph. Ultimately, this would lead to increased costs for tax payers who for the most part are also Guelph Hydro's rate payers.

We suggest revising the ARC to reflect three key purposes:

- The prevention of cross-subsidies between the LDC and its affiliates;
- The protection of individual rate payer information by the LDC; and
- The prevention of any unfair advantage given by a regulated LDC to an affiliated entity <u>if</u> there is another entity interested in competing for the business.

Under the present ARC, the public and ratepayers are incurring extra costs and giving up economies of scope and scale to preserve a hypothetical opportunity for competition.

Communicating with Rate Payers

While the Government has in the past taken a direct hand in designing bills, we would encourage the OEB to take leadership and accept our support in overhauling the current billing format. Our independent research has found that rate payers consider their bills to be ineffective and confusing. This is hardly surprising as they are largely incomprehensible to most consumers. In our research, Guelph Hydro found that rate payers want a short invoice, with more details available on request. Customers should be able to understand the generic categories of cost that form their bill, and particularly, to see quickly and clearly what items the rate payer can control and what are beyond their control. This reform will also improve customer understanding with the electricity industry as a whole, because frequently, customers complain about "high" bills when the real problem is the confusing long list of charges.

For example, (other than water or wastewater services which are quite normal) given that the LDC is the only entity identified on the bill, each bill should clearly set out the following:

- The portion of the bill that is for the service provided by the distributor;
- The portion represented by the commodity price of electricity; and
- All other expenses that contribute to the overall price of electricity.

Guelph Hydro would be pleased to participate in an OEB review of the rate payers' bill format.

We commend the OEB for its long-standing customer communications efforts and encourage you to build on that initiative. While we each have our own brand, the OEB's is very important to the entire electricity industry and in public outreach functions, our ability to help support your brand should not be overlooked. The OEB could remind customers on every bill about areas that it regulates and others, such as smart meters, that are created by the legislature, or otherwise unregulated.

We also suggest that the OEB consider issuing plain language documents outlining their decisions, and have those aimed at the general public. The OEB's regulatory scrutiny is a valuable service provided to the public. However, given the highly technical nature of the OEB's written reasons and their legal context, they are rarely considered or understood by the public at large. Written reasons for decisions are appropriate for experts and lawyers but ineffective for communicating with rate payers. The insurance industry, faced with a similar challenge of being precise for legal reasons but understandable to its customers, has put considerable effort into achieving both aims and their efforts might serve as a model for the OEB.

These proposed changes should reduce long range costs for the whole electricity industry, including the OEB, by reducing friction with customers and providing a regulatory process that is more accessible, efficient and effective for the public.

Intervenors

We understand the importance of evidence presented both pro and con in an application submitted to the OEB. We furthermore understand that there will be costs to marshalling and presenting the con evidence whether in the form of intervenor costs, costs for OEB staff or, as in some jurisdictions, to fund a statutory consumer advocate. In this context, we are generally supportive of the current intervenor process. However, we do see the need for the OEB to impose greater control on intervenors and cost awards to ensure fairness to the rate payers. Again, this is an issue of ensuring costs are more than offset by benefits.

Guelph Hydro suggests that before its rate payers are compelled to pay costs for an intervenor that might have no connection with Guelph, and no understanding of our customers' desired balancing of service and cost, the intervenor should be required to show that its membership includes a substantial number of customers within Guelph Hydro's service territory. Furthermore, the OEB should review its criteria for cost awards and consider including an assessment of the value provided by an intervenor on a hearing by hearing basis. It is clear that many intervenors bring in valuable information, data and suggestions which are helpful to the OEB and the applicant and therefore serve customers interests well. But it is also clear that others are needlessly repetitive and are participating as a matter of course rather than with any clear objective or constructive contribution in mind.

Sincerely,

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