McCarthy Tétrault LLP
Box 48, Suite 5300
Toronto Dominion Bank Tower
Toronto ON M5K 1E6
Canada
Tel: 416-362-1812
Fax: 416-868-0673

George Vegh
Direct Line: 416 601-7709
Direct Fax: 416 868-0673
Email: gvegh@mccarthy.ca

December 7, 2012

Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, Suite 2700
Toronto ON
M4P 1E4

Dear Madame:

Re: Renewed Regulatory Framework for Electricity Report (the "Report")
Board File No.: EB-2010-0377; EB-2010-0378; EB 2010-0379; EB-2011-0043 and EB-2011-0004

Introduction

This letter is written in my capacity as Chair of the Distribution Regulation Review Task Force (the "Task Force"). The Task Force is an initiative of the leading gas and electricity distribution utilities in Ontario aimed at encouraging thought and discussion on how the Ontario Energy Board's ("OEB" or the "Board") approach to regulating energy distribution can be enhanced. These utilities are: Enersource Hydro Mississauga Inc., Horizon Utilities Corporation, Hydro Ottawa Limited, PowerStream Inc., Toronto Hydro-Electric System Limited, and Veridian Connections Inc., Enbridge Gas Distribution Inc., Hydro One Networks Inc., and Union Gas Limited.

The Task Force has supported and participated in all stages of the Board's consultations respecting the Renewed Regulatory Framework for Electricity Distributors and Transmitters ("RRFE") and attended the Board's Information Session on October 31, 2012.

In the Task Force's view, the RRFE was necessary to address the most pressing need in the sector – an improved approach to the rate treatment of investment required for infrastructure renewal. As the Chair of the OEB has observed, "one of the major challenges facing the sector today and the most significant driver of costs is the scale of capital spending expected over the next few years from most utilities – generators, transmitters and distributors alike – to renew and modernize the system and provide for new demand."[1]

The Task Force appreciates that the Board has established Working Groups to further develop the implementation framework for the three options, and its members look forward to providing constructive input to that process. Nevertheless, there does not appear to be a specific process aimed at addressing a particularly important but still outstanding issue, that is, the treatment of infrastructure investment in the Incremental Capital Module ("ICM") within the context of the 4th Generation Incentive Regulation Mechanism ("4th Generation IRM").

The Task Force therefore requests that the Board provide a forum where stakeholders can specifically engage in discussions respecting the ICM criteria, and how they can be interpreted and applied. This can be addressed within the context of current ICM applications (i.e., by treating their outcomes as resolving industry wide generic issues) or through a working group process that can lead to a supplemental report.

The Need for Clarity for 4th Generation IRM

In different decisions, reports and guidelines, the Board has applied a number of different criteria for an investment to qualify for Incremental Capital Module ("ICM"); these are:

- "Materiality, Need and Prudence"[2]
- "Materiality, Need and Prudence", **plus** "extraordinary and unanticipated"[3]
- Materiality, Need and Prudence", **plus** "extraordinary"[4]
- "Applicants must demonstrate that the amounts exceed the Board's materiality threshold and clearly have a significant influence on the operation of the distributor, must be clearly non-discretionary and the amounts must be outside the base upon which rates were derived. In addition, the decision to incur the amounts must represent the most cost-effective option for ratepayers."[5]
- "Discrete, Material and non-discretionary" and, apparently, facility specific.[6]

---

[1] Rosemarie T. Leclair, Chair & CEO, Ontario Energy Board, Remarks for the Ontario Energy Network, November 21, 2011, p. 7.

[2] Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, July 14, 2008, s. 2.5; see also, Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, September 17, 2008, Appendix B.

[3] Hydro One Networks Inc. Decision, May 13, 2009 (EB-2008-0187).

[4] Oshawa PUC Decision, June 10, 2009 (EB-2008-0205).

[5] Guelph Hydro Electric System Inc., Decision, May 13, 2009 (EB-2010-0130 (corrected)) June 10, 2009; and Oakville Hydro Electricity Distribution Inc., Decision (EB-2010-0104), June 10, 2009.

[6] Toronto Hydro-Electric System Limited (EB-2011-0144), Decision, January 5, 2012. The decision referred to the fact that municipal transformer stations have been funded through ICM and suggested that an IRM application that requested

These different approaches have left all parties with considerable uncertainty as to how the ICM criteria will be interpreted and applied. As a result of this uncertainty, the Task Force – whose members are responsible to make necessary investments in infrastructure renewal - requested that the Board conduct a specific process to bring clarity and direction to this important issue.

Unfortunately, the Report did not provide specific direction in this regard. Instead, the Report referred to another Board document – the *Filing Requirements for Electricity Transmission and Distribution Applications* (the "Filing Requirements"). The entire treatment of this issue in the Report is as follows:[7]

> "In the Filing Requirements issued in June 2012, the ICM was further revised to remove words such as 'unusual' and 'unanticipated' as prerequisites to an application for incremental capital, although the requirement that the proposed expenditures be non-discretionary remains."

With respect, this statement raises as many questions as it answers.

First, the reference to the Filing Guidelines does not provide a clear statement of OEB policy and does not provide assurance as to what criteria a panel will apply. The Filing Guidelines only set out minimum evidentiary requirements that must be filed to support an application. They are expressly not a statement of OEB Policy; indeed, they provide that they do "not preempt the Board's discretion to make any order or directive as it determines necessary concerning any of the matters raised by the applications filed."[8]

Second, even if the Filing Guidelines did clarify *which* criteria will apply, it is still necessary to clarify *how* a specific criterion will be interpreted and applied. Of particular concern is the Report's reliance on the term "non-discretionary" to describe the spending that can qualify for ICM treatment. That term is open to a number of different meanings. In the context of transmission investments, the Board has provided at least some illustrations of projects that may be considered "discretionary" and "non-discretionary".[9] However, even that limited level of guidance is not provided for distribution investments.

Conclusion

The Task Force therefore requests that the Board provide a forum where stakeholders can specifically engage in discussions respecting the fundamental ICM criteria, and how they can be interpreted and applied. This can be addressed within the context of current ICM applications (i.e., by treating their outcomes as resolving industry wide generic issues) or through a working group process that can lead to a supplemental report.

Further, the Report provides that the term of the 4th Generation IRM should be extended to 5 years (rebasing plus 4 years). This term extension is extremely challenging because it defers the

---

funding for similar facilities would be "directly analogous to projects that the Board has previously approved under ICM for other distributors." (at p. 22).

[7] Report, p. 18.

[8] Filing Guidelines, pp. 1-2.

[9] Filing Guidelines, pp. 9-10.

period of rebasing – particularly in relation to rate base additions. This leads to greater uncertainty over cost recovery and increased step change rate adjustments upon rebasing. This challenge is exacerbated by the uncertainty with respect to the ICM.

Although this issue was floated by some participants in the consultation process, it is fair to say that there was not a detailed consideration of the costs and benefits of this approach. The Task Force therefore respectfully requests that the appropriate term of the 4th Generation IRM be an issue for further consultation.

Sincerely,

signed in the original

George Vegh,

Chair, Distribution Regulation Review Task-Force

c: Norm Ryckman, Michael Lister – Enbridge Gas Distribution Inc.
Gia DeJulio – Enersource Hydro Mississauga Inc.
Indy Butany-DeSouza – Horizon Utilities Corporation
Ian Malpass – Hydro One Networks Inc.
Jane Scott, Patrick Hoey – Hydro Ottawa Limited
Colin Macdonald, Sarah Griffiths – PowerStream Inc.
Colin McLorg – Toronto Hydro Electric System Limited
Mark Kitchen – Union Gas Limited
George Armstrong – Veridian Connections Inc.