BACKGROUND

The Federation of Rental-housing Providers of Ontario (FRPO) appreciates the opportunity to be involved in the Board's consultation on the Performance of Electric LDC's. FRPO had its first involvement in electricity regulation at the policy level in Renewed Regulatory Framework for Electricity. We have yet to be involved in any utility specific rate case. As such, it is difficult to draw on rate case experience to draw practical conclusions on the applicability of some of the experts' proposals. We also did not engage for ourselves an econometrics expert. Therefore, we are not equipped to do a qualitative assessment of the expert reports and will, instead, constrain our submissions to a higher level review.

Inflation Factor

We were enlightened by the experts' respective views on how to assess inflation in attempts to meet the Board's policy direction. A common theme in the approaches were measures to mitigate volatility. In our submission, we would support the continued use of GDP IPI FDD. It is a tried and tested measure that has been shown[1] to mitigate this issue of volatility that the other proposed measures were trying to address. From our review of the 2011 Yearbook of Distributors, it seems to be working.

[1] OEB Board Staff Paper on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, dated February 28, 2008, pages 53-56

The Productivity Factor

Once again, the experts had competing econometric approaches to try to deal with the productivity factor. Each of the experts provided qualitative assessments of macroeconomic factors that contributed to their choice of inputs and resulting measures. Some conjectured whether recent history is indicative of the future conditions and made adjustments as a result. Most provided constructive reasoning why other expert's analysis may produce a skewing of results. Each expert also provided a level of theoretical support to substantiate their own approach as the most effective methodology.

We are not equipped to enter the debate to say which approach is the best. However, there were aspects of some that, in our view merit attention. The submissions by the Coalition of Large Distributors (CLD) model brought in more inputs than proposed by the PEG approach which we believe could be effective as a management tools to determine drivers of efficiency. However, we have come to believe that there are challenges with this model also.

Submissions from the Power Works' Union (PWU) brought in Line Losses and Reliability. While we cannot comment on the relative merit of this approach versus other propositions, we do acknowledge the importance of this issue. FRPO does support a further study of these issues. Given the focus on the experts' debate on econometrics, what seemed to get lost, from our perspective, is that Performance clearly has a service quality component. If incentives embedded in this generation of regulation create conditions that reduce maintenance resulting in increased Line Losses and reduced Reliability, we ought to understand these implications. What we had hoped to read was that Line Loss reduction incentives had a direct impact (beyond the anecdotal case cited from Alberta) and, if we had, would have been more

supportive of this approach. If that effect has been studied and proven in another jurisdiction, we believe it is worthy of pursuit. At the very least, we would expect that the development of the balanced scorecard could address these issues but there would need to be appropriate incentives tied to those results especially if they incent improved performance.

Given our inability to support one model and its output value for an Ontario electricity distribution Total Factor Productivity trend, we offer an alternative approach that has been used on the gas side of Ontario utility regulation with Enbridge Gas Distribution. We would recommend that the productivity factor be an established percentage of inflation (eg., 40% of inflation). Said another way, in our proposal, the utility would be able to use 60% of the GDP IPI FDD for annual rate increases. Beyond removing the debate and potential unintended consequence of one TFP set number that is constant, this approach would be robust in uncertain inflationary times ahead. We understand that it is not directly a TFP approach. However, the Board could use the range of TFP's from the models to establish the appropriate percentage as the Productivity Factor (or range of Factors as discussed below in the next section).

Efficiency Cohorts/Rankings & Stretch Factors

The only topic that seems more controversial than the approach to TFP was the approach of establishing cohorts and their rankings. We would support the submissions of the School Energy Coalition (SEC) in using the knowledge of the utilities themselves to improve the

establishment of the cohort. In the technical conference[2], SEC advanced the concept of allowing utilities to "vote" with other utilities on who they benchmark themselves against. We think the concept has merit but we will leave the detailed explanation to the SEC submissions. Having an opportunity to preview some of their submissions, FRPO supports SEC's ideas on utilities contributing to the development of their cohort.

Once the cohorts are established and rankings are determined through Total Cost Benchmarking, we would propose to extend the simplified productivity approach into a range that would produce stretch factors. Using the rankings within the cohort, levels of stretch could be created that are additional to the Productivity Factors. We would propose 5 levels to allow for movement based upon performance. Extending the example of using a 40% productivity factor, the five levels could be assigned 0%, 5%, 10%, 15%, 20% ranked from the best cost performer to worst. Therefore, the best cost performer is rewarded with 0% stretch factor resulting in a combined 40% productivity and stretch factor or an increase based upon 60% of GDP IPI FDD. Conversely, the worst performer would be applied a 60% combined productivity and stretch factor and would only be allowed to increase rates by 40% of the GDP IPI FDD. We have provided the numbers as examples and, if the Board found this methodology effective, the percentage chosen could be informed by the significant data and analysis expected to be generated in this proceeding.

[2] Transcript, Stakeholder Conference, Volume 2, May 28, 2013, pages 100-2

Implementation Considerations

We appreciate that any model chosen has its limitations and periodically unintended consequences. We support the Board's concern for performance +/- 300%. From our review of the 2011 Yearbook of Electric Distributors, it is clear that more distributors are able to achieve their approved ROE and the outliers are diminishing (versus 2007). We would encourage the Board to consider a further intra-period adjustment that could buffer variability around the approved rate of return. A further percentage adjustment could be integrated into the ratemaking process that would add or subtract 5% points to the annual increase based upon the last year's performance.

For example, if a utility's actual return is within 100 basis points of its approved rate for that year, no further adjustment is necessary. However, if the utility over earns between 100 and 200 basis points a 5% adjustment is applied to the combined productivity and stretch factor components. From the previous example, if the best performer had a combined 40% combined productivity and stretch factor and the utility over earned by 150 basis points, 5% would be added to its factors resulting in an allowed increase of 55% of the GDP IPI FDD. Similarly, if that same utility under earned by 250 basis points, an adjustment of 10% would be deducted from the 40% productivity and stretch factor resulting in an allowable increase of 70% of the GDP IPI FDD. While it is clear that this method would incorporate a time lag tied to production of year-end statements, it does provide the utility and ratepayers with intra-period protection that could reduce the risk of a +/- 300 basis point performance resulting in a rate case.

We trust that while our concepts are simple, the result would be a dampening mechanism to allow LDC's to operate during the IRM period while striving to incent improved performance and adjust rate-setting parameters intra-period.

All of which is respectfully submitted on behalf of FRPO,

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