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May 5, 2014

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

Dear Ms. Walli:

Re: EB-2014-0138 – Review of the Board's Policies and Processes to Facilitate Electricity Distributor Efficiency: Service Area Amendments and Rate-Making Associated with Distributor Consolidation - Comments of the London Property Management Association

Please find attached the comments of the London Property Management Association related to the above noted proceeding.

Sincerely,

Randy Aiken

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Aiken & Associates

A. INTRODUCTION

In the March 31, 2014 letter re: ***Review of the Board's Policies and Processes to Facilitate Electricity Distributor Efficiency: Service Area Amendments and Rate-Making Associated with Distributor Consolidation***, the Board invited stakeholders to comment on the staff Discussion Paper. The Board's letter indicated that stakeholders should feel free to comment on all issues addressed in the Discussion Paper in addition to providing responses to the questions identified. The Board also indicated that parties should identify any preferred alternatives for addressing the issues.

These are the comments of the London Property Management Association ("LPMA") with regard to Service Area Amendments and to Rate-Setting Associated with MAADS.

As a general comment, LPMA notes that the goal of the facilitation of electricity distributor efficiency should be to ensure ratepayers are paying just and reasonable rates. It should not be about higher returns to the owners of those electricity distributors over an extended period of time.

B. SERVICE AREA AMENDMENTS

a) General Comments

LPMA submits that the determination of service area amendments should be made on the basis of what is best for ratepayers. In this context, ratepayers means the current ratepayers of both the Incumbent Distributor and the Applicant Distributor and any new ratepayers that will be located in the "un-serviced area", as defined in the Discussion Paper.

In the example provided in the Discussion Paper of an Applicant Distributor that wants to provide a connection to a new subdivision where the Incumbent Distributor does not have the capacity to provide service, LPMA notes that this could generally be interpreted to mean that the Applicant Distributor can provide the necessary assets to provide the needed capacity at a lower cost than the Incumbent Distributor, which may have to extend lines farther than the Applicant Distributor, or enhance the capacity of upstream lines.

In this example, there are three groups of customers. The new customers in the subdivision to be served; the existing customers of the Incumbent Distributor and the existing customers of the Applicant Distributor. LPMA submits that the impact on all three groups of customers should be taken in account in the determination of which distributor should provide service.

LPMA submits that an economic evaluation calculation should be done by both the Incumbent and Applicant distributors. The resulting shortfall (or surplus) should then be compared against one another. The proposal with the lowest shortfall (or highest surplus) would normally be the distributor that would be approved to serve the area in question as it would be the least cost provider.

This would ensure that the impact on the existing customers of the two distributors would be the addition of the smallest shortfall, or the largest surplus. Such a calculation would need to cover all costs, so as to reflect not only differences in asset costs (including gross asset costs, capital costs and PILs), but also in OM&A costs between the two distributors.

b) Response to Staff Questions

Question 1 - *What are the benefits of an "open for competition" approach to un-serviced areas? How would the Board implement such an approach in light of section 28 of the Electricity Act, 1998 and existing licence conditions? Under an "open for competition" approach: (i) how will the Board ensure that all prospective new customers will receive an offer to connect on fair and reasonable terms; and (ii) how should the interests of Incumbent Distributors and their ratepayers be taken into consideration?*

The benefits of an "open for competition" approach to an un-serviced area have been discussed in the general comments above. The distributor that can serve an un-serviced area at least cost to ratepayers should be awarded the un-serviced area. Of course, minimum service quality would need to be maintained.

As a condition for receiving the service area, the distributor should be required to make an offer to connect on fair and reasonable terms to all prospective new customers.

LPMA submits that the interests of Incumbent Distributors and their ratepayers are taken into consideration through the use of the "open for competition" approach. The Incumbent and Applicant distributors (and their ratepayers) should be treated equally. Just because an un-serviced area resides in the service territory of one distributor and not another should not be a determining factor, especially since there may not have been any good reason for it being included in the service area for one distributor versus another.

Question 2 - *Should the Board's SAA policy facilitate SAAs that have the effect of aligning a distributor's service area with municipal planning boundaries and, if so, in* *what way? What are the benefits and risks of such an approach for Incumbent Distributors, Applicant Distributors and their respective ratepayers? What role should municipal planning, community energy plans and regional planning have in the SAA process?*

LPMA does not believe that the Board's SAA policy should be influenced by the effect of aligning a distributor's service are with municipal planning boundaries.

The risks of doing so could insert additional costs into the system that would be based on artificial boundaries rather than basing the service areas on economic conditions. Since most municipal boundaries coincide with roads, the implication is that there would be many roads in Ontario with hydro lines running down both sides of the roadway with two distributors serving different municipalities. This duplication of costs is just one example of what happens when artificial boundaries are imposed on the industry.

Municipal planning, community energy plans and regional planning should be used as a key input to determine which distributor is best situated to serve a contested area. However, all of the planning would continue with both distributors, regardless of which distributor serves a particular area or subdivision because of the close proximity of the two distributors. This is similar to municipal planning that has to take into account the planning of the neighbouring municipality.

Question 3 - *For either proposed change to the Board's current policy: (i) How should the Board approach its analysis? (ii) What criteria should be used by the Board and what type of evidence would be necessary? (iii) How can the Board ensure that the proposed change would not adversely affect overall economic efficiency in the sector? (iv) How should the Board assess the impact on existing and future customers in terms of cost and the reliability and quality of electricity service? (v) How can the Board be satisfied that the process will ensure that the connection of new customers proceeds in a timely manner?*

The economic evaluation methodology proposed above in the general comments provides a basis for the Board to approach its analysis. The criteria and type of evidence that would be necessary is all of the information for the alternatives to be considered. This would be similar to a leave to construction proceeding for natural gas distributors, except both distributors would provide evidence as to why their proposal is the best alternative for ratepayers. The proposed approach would ensure that the least cost option would be approved, unless there were mitigating circumstances.

LPMA does not believe that reliability and quality of electricity service impacts are likely to be significant on existing and future customers. This would only be the case if there was a wide difference between the competing distributors in the quality and reliability of service. In most cases this difference is not likely to be significant. In situations where there is a wide difference, the Board could evaluate this difference, similar to a stage 2 or stage 3 analysis in a natural gas leave to construct application.

To ensure the timely connection of new customers, LPMA submits that the municipal and regional planning should identify all such service areas that may be contested in the near future. If the distributors cannot agree among themselves as to who should serve the area, then an application should promptly be made to the Board. The Board should also look at ways it could speed up the regulatory process to ensure no delays for new customers.

C. RATE-SETTING ASSOCIATED WITH MAADS

a) General Comments

LPMA submits that any rate-setting policy associated with MAADs should be focused on the benefits to ratepayers. It is the ratepayer that must ultimately benefit in the long run from the approval of any MAADs application. The question is how much of the savings from a merger or acquisition need to be re-directed to a shareholder from ratepayers in order to entice the shareholder to do the deal.

i) An Alternative

LPMA notes that the Staff Discussion Paper is focused on rebasing deferrals for consolidated entities. LPMA submits that this is burdensome from a regulatory point of view and that a simpler approach that has the same end result is available.

In particular, an alternative approach to a rebasing deferral period to allow a consolidated entity to recover its merger and acquisition costs would be to allow the consolidated entity to recover these costs directly through a rate rider. The costs would be amortized over a number of years (to be determined) and would be independent of whatever rate-setting methodology was in place for the various parts of the consolidated entity.

This would not require any rebasing deferral period and would allow the consolidated distributors to move forward with rate harmonization on a faster basis than if rebasing is deferred.

A version of this alternative approach would be to allow the consolidated entity to recover not only the merger and acquisition costs, but also an incentive to proceed with the merger in order to encourage mergers. This higher amount would continue to be recovered through a rate rider, but would be in place for a longer period of time.

ii) Timing of Rebasing

In addition to the above, LPMA notes that the Discussion Paper indicates that there will now be potential for distributors that are party to a MAADs transaction to be on different rate options at the time of consolidation (Custom IR, Price Cap IR and Annual Index). Staff state that it would be consistent with the 2007 policy for distributors that are on the Price Cap option at the time of consolidation to continue to have their rates adjusted under that same mechanism until rebasing.   LPMA agrees that this is appropriate.

Similarly, LPMA submits that a distributor that is on the Custom IR option at the time of consolidation should continue to have their rates set based for the duration of the Custom IR plan as determined by the Board.

LPMA notes that the Staff Discussion Paper does not address the timing issues related to the consolidated entity and the time horizon for rebasing of the merged distributors. For example, one of the merged distributors could be on a Custom IR plan with rates set for 2016 through 2020, while the other merged distributor could be on another plan (Custom IR or Price Cap IR) with rates set under these options for 2018 through 2022. LPMA notes that the use of the Annual Index method to set rates does not appear to pose any issues in terms of the timing of rebasing since there is no set rebasing timeframe.

It is not clear how the rates for the first of the merged distributors in the above example would be set for the bridge period of 2021 and 2022. One of the merged distributors has its rates set for these two years, but the other does not. The ones that does not could not do a Custom IR or a Price Cap filing for two years since this would not be consistent with the policy that these applications are for a minimum of five years.

LPMA submits that if there is only year between the ending points of the timeframes, the Annual Index method should be used for the merged distributor that needs to set rates for an additional year before rebasing for the consolidated entity can take place.

If the difference between the two is more than one year, the Board should consider allowing the use of the Price Cap adjustment for the distributor that needs to set rates for these additional years before the rebasing of the consolidated entity can take place.

b) Response to Staff Questions

Question 1 - *What are the merits and risks of allowing a consolidated entity to set its own rebasing deferral period? Should the Board establish a "default" minimum deferral period and, if so, what should the length of that deferral period be? Should the consolidated entity be required to elect its rebasing deferral period at the time of the MAADs application (as is the case under the 2007 Policy), or should the entity be allowed to address this at a later date and, if so, when? What information should a consolidated entity provide to support its proposed rebasing deferral period?*

LPMA notes that the issue for distributors and their shareholders is a rebasing deferral period that is long enough to allow them to recover their merger and acquisition costs, at a minimum. For some distributors this would be enough for their shareholders as they would want to pass the ongoing savings that result from the merger onto their ratepayers as soon as possible. For others, they will want a further shareholder incentive to be enticed into a merger before they pass the savings onto their ratepayers.

LPMA submits that the consolidated entity should be allowed to set its own rebasing deferral period. This comes with a number of caveats. First, the consolidated entity should provide a forecast of how long it expects to take to recover its merger and acquisition costs through planned savings. Second, based on its requested deferral period, there should be a forecast of the savings that would accrue to the consolidated entity before the next rebasing. Third, and most importantly, the actual costs and savings should be tracked in a deferral account and at the subsequent rebasing, there should be a sharing of the net savings that have accumulated in the account.

LPMA does not believe that a minimum deferral period should be set as a default. If a distributor believes it can recover its merger and acquisition costs in a short period of time and wants to pass any further savings onto ratepayers immediately, it should be allowed, and indeed encouraged, to do so by the Board. On the other hand, LPMA believes that the Board should set a default maximum deferral period. This maximum deferral period should not be determined until the Board has some experience with the forecasts provided from distributors as to how long they expect to take to recover their costs and the forecasts of further savings.

A consolidated entity should be required to elect its rebasing period at the time of MAADS application, consistent with the 2007 policy. LPMA is not aware of any change in circumstance that would suggest a change to this policy is necessary.

As noted above in the general comments section, LPMA suggests that a deferral account and a rate rider to recover the merger and acquisition costs and, if necessary, an incentive to merge, would be a preferable approach. Under this approach, the consolidated entity is guaranteed to recover their costs and, if applicable, their incentive. At the same time, ratepayers would pay a fixed cost for the merger and would not forego possible savings in excess of the incentive.

As well, the rebasing application would not need to be deferred. This would deal with the issue of capital expenditures raised in the consultation by some distributors as there would be no difference in the timelines with or without a merger. The consolidated distributor would also be able to deal more quickly with rate harmonization. Ratepayers would be able to more quickly realize the savings from the merger through their rates.

Question 2 - *Once a consolidated entity has proposed a rebasing deferral period, should it be required to wait for the entire period before applying for a rebasing of its rates, or should it be allowed to apply for rebasing at any time within the proposed period? What are the merits and risks of each approach?*

LPMA submits that a consolidated entity should be able to request a rebasing of its rates before the requested deferral period is over, but only under certain circumstances. For example, as noted above, the distributor may want to pass on savings through lower rates to their ratepayers if the merger savings are higher than expected.

On the other hand, if the savings resulting from the merger are less than expected, the consolidated entity should not be allowed to ask for a rebasing to pass through higher costs . The entity should be expected to continue to seek savings from the merger and not take the easy way out if their original estimates were too optimistic.

Question 3 - *In the case of a distributor that is on Custom IR at the time of consolidation, how should its rates be set for the duration of the rebasing deferral period following completion of the Custom IR period?*

As noted above, the use of a deferral account and rate rider over a specific number of years would eliminate this issue. The rebasing would not need to be deferred as the costs and incentives would be recovered through a rate rider independent of when rebasing occurs. There would not need to be any special rules for when a consolidated entity that is on Custom IR at the time of consolidation following completion of the Custom IR period.

<u>Question 4</u> - *What are the merits and risks of the suggestion that a newly consolidated entity apply for new rates under the Custom IR option that recognize both costs and projected efficiency savings, (e.g. an efficiency carryover to allow the distributor to recoup transaction costs)? Is this complimentary to or a substitute for an approach that allows the deferral of rebasing?*

As noted above, the alternative mechanism of a deferral account and a rate rider to recover the costs and keep some of the efficiency savings would work irrespective of whether the consolidated entity is under Custom IR, Price Cap IR, or Annual Index.

LPMA further notes that the consolidated entity may, in fact, be under more than one type of regulation. One of the merged distributors could be under Price Cap IR and the other under a Custom IR.

LPMA believes that this is a substitute for the deferral of rebasing.

<u>Question 5</u> - *What are the merits and risks of using a modified ICM (which allows broader eligibility of expenditures) to address the recovery of capital investments during any rebasing deferral period? How should the Board evaluate an ICM request under this scenario to ensure that any financing is for investments that are incremental to the capital amount built into rates?*

The obvious risk associated with using a modified ICM is that the impact on ratepayers could be worse than if no merger took place. The ICM mechanism does not take into account merger savings or reduced cost of capital, as was suggested by the Distribution Sector Review Panel would result from consolidation.

Under the deferral account and rate rider approach noted above in the general comments, the ICM module would continue to be available to the consolidated entity if it was under the Price Cap IR.

LPMA notes that this approach appears to be simple and straightforward. The regulatory burden of such an approach is significantly less than dealing with rebasing deferrals, which can become quite complicated if one merger or acquisition in one year is followed by a merger with another entity before the rebasing deferral period expires.

The rate setting models (Custom IR, Price Cap IR and Annual Index) are not impacted by the recovery of the merger and acquisition costs and the recovery of any incentive.