Ontario Energy Board | Commission de l'énergie de l'Ontario

November 29, 2018

Report of the Ontario Energy Board

Energy Retailer Services Charges

EB-2015-0304

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EXECUTIVE SUMMARY

This Report sets out the conclusions of the Ontario Energy Board (OEB) following the OEB's review of energy retailer service charges for electricity and natural gas distributors.

The OEB has determined that, due to the operational differences that exist between the electricity and natural gas sectors, it is not appropriate to establish standardized energy RSCs[1] that would apply equally to both electricity and natural gas distributors. The OEB has also determined that the service charges for natural gas distributors will not be adjusted given that the current charges continue to closely track costs. However, adjustments to the electricity RSCs are warranted to ensure that revenues are more closely aligned with the costs of providing services to electricity retailers. The OEB continues to be of the view that default electricity RSCs remain appropriate.

Energy retailer service charges refer to the charges that recover the cost of services provided by electricity and natural gas distributors to electricity retailers and natural gas marketers (collectively referred to as energy retailers) or to customers, related to the supply of competitive electricity or natural gas. Energy retailers offer consumers retail contracts with varied terms or offerings such as the opportunity to buy their energy at a fixed price for the term of the contract. Examples of services provided by electricity and natural gas distributors are the establishment of service agreements, billing and other transactional activities.

Retail service charges (RSCs) for electricity distributors were established by the OEB in 2002 with the opening of the competitive electricity market. At the time, the OEB reviewed practices in other jurisdictions and developed a set of default values for electricity distributors to charge for retail services with the understanding that the actual costs for providing these services may differ across distributors. These default values for electricity RSCs have not been reviewed since they were established. Natural gas distributors also have service charges but they are distributor-specific. These service charges have not been reviewed in the recent past, either. As a result, the OEB decided to proceed with a review of energy retailer service charges for both sectors.

The scope of the review also included an examination of the methodology to reset the energy RSCs and mechanisms for keeping these charges up to date. The review also examined the establishment of a new service charge for electricity and natural gas

[1] When the service charges for electricity and natural gas distributors are collectively referred to in this Report, they will be referred to as "energy retailer service charges" or "energy RSCs". Electricity RSCs refer to service charges for electricity distributors only.

distributors to recover the transactional costs of sending a “notice of switch” letter to low volume customers who signed a contract with an electricity retailer or gas marketer. The OEB established a working group to assist with the energy RSCs review.

A Draft Report of the OEB (Draft Report) was issued for comment on July 19, 2018. The OEB received nine letters of comment from interested stakeholders including electricity distributors, natural gas distributors, and energy retailers.

Through this review, it has become apparent that the current electricity RSCs, which were established approximately 16 years ago and have not been updated since then, do not recover the costs associated with providing services to electricity retailers. Currently, revenues collected from energy retailers cover about less than half the costs incurred to provide service. This under-recovery of costs means that ratepayers are cross-subsidizing energy retailers. While concerns were raised about the level of adjustment to the electricity RSCs proposed in the Draft Report, the OEB notes that energy retailers have benefited for several years from lower electricity RSCs given there have been no changes to them since they were established. The adjustment is an appropriate step in addressing the current cross-subsidization that exists, and is therefore in the public interest. The OEB will therefore proceed to adjust the electricity RSCs, except for the one-time Retail Service Agreement Charge.

The OEB intends to implement the updated electricity RSCs on May 1, 2019. The electricity RSCs will subsequently be adjusted annually commencing on January 1, 2020 based on the OEB’s inflation factor. Natural gas distributor RSCs will also be adjusted annually commencing on January 1, 2020 based on the OEB’s inflation factor. The OEB will not require any adjustments to the Agent Billing and Collection charges of Enbridge Gas Distribution Inc. (Enbridge Gas) as they are structured as a non-utility service.

The OEB will establish a new one-time energy retailer service charge for both electricity and natural gas distributors of $2.00 to recover the incremental cost of sending a notice of switch letter to low volume customers who sign a contract with an energy retailer. The new service charge will apply only to letters that are sent by standard hard copy mail. The new charge will be adjusted annually similar to all other energy RSCs commencing on January 1, 2020. After considering the comments on the Draft Report from electricity distributors, natural gas distributors, and energy retailers, the OEB believes that setting the notice of switch charge at $2.00 remains appropriate. However, the OEB will allow electricity and natural gas distributors the option to opt out of applying the charge to energy retailers.

The OEB will proceed with the elimination of the Retail Service Cost Variance Accounts (RCVAs) as outlined in the Draft Report. The OEB will, however, allow electricity distributors who are still using the RCVAs to continue doing so until rebasing in light of concerns raised by electricity distributors on the potential financial disadvantage the immediate elimination may cause electricity distributors that are still using the RCVAs. At market opening, there was uncertainty about the cost of the settlement process with electricity retailers. This settlement process has now been an integral part of the operations of electricity distributors for more than 16 years. At rebasing, the balances will be disposed of and the RCVAs will be eliminated. Electricity distributors with a longer deferral period prior to rebasing can ask for disposition of the RCVAs prior to rebasing if the amounts in the RCVA are significant, however, the RCVAs will remain open until rebasing. The OEB does not see merit in electricity distributors continuing to track these variances beyond rebasing.

The increase in the electricity RSCs in the midst of an incentive rate-setting term will result in revenues earned being greater than amounts previously approved in an electricity distributor's distribution rates. As outlined in the Draft Report, a new variance account will be established for electricity distributors. However, this new variance account will now only apply to electricity distributors who no longer use the RCVAs. The new variance account will be disposed of and eliminated in an electricity distributor's future rate application.

The updated electricity RSCs are shown in the table below.

Table ES 1: Current and New Electricity Retail Service Charges

Electricity RSCs	Unit	Current Charges	New Charges
Retailer Service Agreement	per agreement (one-time)	$100.00	**No Change**
Monthly Fixed Charge	per retailer (monthly)	$20.00	**$40.00**
Monthly Variable Charge	per retail customer (monthly)	$0.50	**$1.00**
Distributor Consolidated Billing Charge	per retail customer (monthly)	$0.30	**$0.60**
Retailer Consolidated Billing Credit	per retail customer (monthly)	$(0.30)	**$(0.60)**
Service Transaction - Request fee	per request	$0.25	**$0.50**
Service Transaction - Process fee	per request	$0.50	**$1.00**
Information Standard Delivery Charge	per request, after 2 free requests	$2.00	**$4.00**

1. INTRODUCTION

On November 5, 2015, the OEB issued a letter announcing that it was initiating a comprehensive policy review of miscellaneous rates and charges applied by electricity distributors for specific services they provide.

These charges generate service revenues that result in lower base distribution rates. Without these revenues, the cost of providing these services would be recovered from all electricity and natural gas customers through distribution rates.

The OEB noted that it would commence the review of miscellaneous rates and charges in phases, beginning with the review of wireline pole attachment charges. On May 31, 2017, the OEB issued a letter announcing that the next phase in its review of miscellaneous rate and charges would be the review of energy RSCs for both the electricity and natural gas sectors. The OEB also announced that the review would examine the establishment of a new service charge for electricity and natural gas distributors to recover the transactional cost of sending a notice of switch letter to low volume customers who have signed a contract with an electricity retailer or natural gas marketer (collectively referred to as energy retailers).

The notice of switch letter was a new requirement implemented following the OEB's review in December 2016 of a broader package of measures to protect consumers in respect of energy retail contracts.[2] The OEB amended the Retail Settlement Code and the Gas Distribution Access Rule to require electricity and natural gas distributors to send a written notice to any low volume consumer who has signed a contract with an energy retailer, confirming that the consumer has been switched to contracted supply. This requirement came into effect on July 1, 2017. In the context of that consultation which included the development of the July 1st requirement, the OEB indicated that it is appropriate for electricity and natural gas distributors to recover the transactional cost of sending a notice of switch letter. The OEB also indicated that the policy review of miscellaneous rates and charges would include the examination of the notice of switch letter.

The letter issued on May 31, 2017 invited stakeholders from the sector to express their interest in participating in a working group as part of the consultation process. The OEB selected participants to be part of a working group led by OEB staff that represented electricity distributors, natural gas distributors, and energy retailers.

[2] Giving Effect to the OEB's Report on the Effectiveness of the Energy Consumer Protection Act, 2010 (EB-2015-0268); Retail Settlement Code section 10.5.4A; Gas Distribution Access Rule section 4.3.10.

On July 19, 2018, the OEB issued its Draft Report for stakeholder comments. The Draft Report was the culmination of the efforts of the OEB and the members of the working group.

A. Background

Electricity RSCs refer to the services provided by electricity distributors to electricity retailers or customers related to the supply of competitive electricity. Default electricity RSCs were established in 2002 when the competitive electricity market was first opened and have never been updated. To establish these charges, the OEB reviewed practices in other jurisdictions and developed a set of default values for electricity distributors with the understanding that the actual costs for providing these services will vary across electricity distributors. These charges are set out in each electricity distributor's Tariff of Rates and Charges. Natural gas distributors levy similar charges for distributor-consolidated billing, contract administration, and bad debt related costs.

Electricity RSCs are grouped into the following three categories: 1) Establishing Service Agreements, 2) Billing and 3) Service Transaction Requests. The current OEB default electricity RSCs are shown in Table 1 below.

Table 1: Current Electricity Retail Service Charges

Category	RSCs	Unit	Charges	Description
1. Establishing Service Agreements	Retailer Service Agreement	per agreement (one-time)	$100.00	Intended to cover costs related to the service agreement between an electricity distributor and electricity retailer.
	Monthly Fixed Charge	per retailer (monthly)	$20.00	
	Monthly Variable Charge	per retail customer (monthly)	$0.50	
2. Billing	Distributor Consolidated Billing Charge	per retail customer (monthly)	$0.30	Intended to recover the incremental costs for an electricity distributor to provide distributor-consolidated billing. A credit is paid to electricity retailers that choose retailer-consolidated billing.
	Retailer Consolidated Billing Credit	per retail customer (monthly)	$(0.30)	
3. Service Transaction Requests	Service Transaction - Request fee	per request	$0.25	Intended to recover the incremental costs of labour, internal information system maintenance costs, and delivery costs.
	Service Transaction - Process fee	per request	$0.50	
	Information Standard Delivery Charge	per request, after 2 free requests	$2.00	

For natural gas distributors, there are no default charges. The charges are distributor-specific. The service charges for Enbridge Gas and Union Gas Limited (Union Gas) are shown in Table 2 below.

Table 2: Current Natural Gas Energy Retailer Service Charges

Category	Energy RSCs	Unit	Enbridge Gas Charges	Union Gas Charges	Description
1. Program Administration	Direct Purchase Admin Charge	Fixed Monthly Charge - per contract	$75	$75	Intended to recover the costs incurred for administrative activities related to gas supply arrangements transacted between the direct purchase contract holder and gas marketer.
		Account Monthly Charge - per account (monthly)	$0.21	$0.19	
2. Billing	Distributor Consolidated Billing Charge	Per retail customer (monthly)	$1.30 per Rate 1 Account $2.00 per Rate 6 & 9 Accounts $5.00 per Rate 100+ Accounts	$0.57	For Enbridge Gas, these charges are not part of the regulated rate setting process. For Union Gas, these charges are intended to recover the costs incurred to allow gas marketers the ability to charge their customers commodity and transportation on the gas bill. Includes an allocation of commodity related bad debt.
3. Miscellaneous Transaction Requests	Invoice Vendor Adjustment Charge	Per transaction	$0.30	$1.09	For Enbridge Gas, these charges are not part of the regulated rate setting process. For Union Gas, the charges are intended to recover the costs incurred to allow gas marketers the option to apply an adjustment on the gas bill.

2. THE CONSULTATION PROCESS

The OEB received expressions of interest from 10 parties to participate in the working group and selected all 10 parties. OEB staff led the working group. The working group was comprised of the following members:

Table 3: Working Group Composition

Electricity Distributors	Member
Guelph Hydro Electric Systems Inc.	Krista Perry
Hydro One Networks Inc.	Danny Relich
Hydro Ottawa Limited	April Barrie
London Hydro Inc.	Martin Benum
Veridian Connections Inc.	Kyle Brown
Natural Gas Distributors	**Member**
Enbridge Gas Distribution Inc.	Rob DiMaria
Union Gas Limited	Tom Byng
Energy Retailers[3]	**Member**
Ag Energy Co-operative Ltd.	Katie Morrow
Just Energy Ontario L.P.	Frances Murray
Summitt Energy Management Inc.	Jeff Donnelly

The OEB held four working group meetings between September and November 2017. At the first working group meeting, OEB staff presented a draft list of topics. Following input received from the working group, OEB staff finalized the list of topics. The final list of topics is included in Appendix A.

At the conclusion of the working group meetings, OEB staff provided an opportunity for working group members to provide written comments on each of the topics. Working group meeting materials and written comments are posted on the OEB's Review of Miscellaneous Rates and Charges webpage.

[3] The three energy retailers who were members of the working group are each licensed by the OEB to retail electricity and market gas and are active in both sectors.

3. THE OEB'S APPROACH

On July 19, 2018, the OEB issued a Draft Report for stakeholder comment. The Report is the culmination of the efforts of the OEB and members of the working group comprised of OEB staff, electricity distributors, natural gas distributors, and energy retailers.

The OEB received nine letters of comment from stakeholders. Letters of comment were received from electricity distributors including the Coalition of Large Distributors[4] (CLD), Electricity Distributors Association (EDA), London Hydro Inc. (London Hydro), and Whitby Hydro Electric Corporation (Whitby Hydro); natural gas distributors (Enbridge Gas, Kitchener Utilities, and Union Gas); and the energy retailers Ag Energy Co-operative Ltd. (Ag Energy) and Just Energy Ontario L.P. (Just Energy).

The comments are posted on the OEB's Review of Miscellaneous Rates and Charges webpage.

This section summarizes the OEB's final approach in each of the following areas:

- Guiding principles
- Province wide versus distributor specific service charges
- Costing methodology and cost elements
- Adjustment mechanism
- Electricity distributor Retail Service Cost Variance Accounts

A. Guiding Principles

Description

The working group members generally agreed that energy RSCs should be guided by the following principles to reasonably reflect the cost of providing service:

- <u>Cost Causality:</u> The service charges should reflect the user pay principle.
- <u>Fairness:</u> The approach should strike a balance between cost causality and simplicity.
- <u>Simplicity:</u> The methodology to re-calibrate the charges should be proportional to materiality. An onerous process is therefore not warranted.

[4] The CLD consists of the following electricity distributors: Alectra Utilities Corporation, Hydro One Networks Inc., Hydro Ottawa Limited, Toronto Hydro-Electric System Limited, and Veridian Connections Inc.

- Flexibility: The methodology should be simple to administer and be adaptable to changing market conditions.
- Minimized Regulatory Burden: The regulatory burden should be reflective of materiality. The revenues associated with the charges should also be easy to forecast.

Stakeholder Comments on the Draft Report

All stakeholders who commented agreed with the guiding principles. One stakeholder indicated that the OEB's principled approach can serve as a framework to guide the ongoing evolution and assessment of electricity RSCs. Another supported the guiding principles established but indicated that including fixed costs in the cost methodology does not reflect the guiding principle of fairness.

The OEB's Approach

The OEB accepts the guiding principles identified by the working group and adopts them for purposes of the updates to energy RSCs. By ensuring that energy RSCs are set at a level that is reflective of cost and by updating these charges periodically, cross-subsidization by ratepayers will be minimized. At the same time, the methodology to reset the charges and keep them up to date should be simple, flexible and not impose an undue regulatory burden on electricity and natural gas distributors. The OEB believes it is appropriate to include both fixed and variable costs as they are reflective of the overall costs incurred to provide service. This is discussed in further detail in Section 3C of this Report.

B. Province-Wide vs. Distributor Specific Service Charges

Description

A "one size fits all" approach was viewed by the working group to be more appropriate for the electricity sector than for the natural gas sector. This is because electricity distributors deliver similar services to retailers and similar costs are incurred. Enbridge Gas and Union Gas did not agree with standardizing the charges across the energy sector, noting that some direct purchase services offered by natural gas distributors were fundamentally different than those offered by electricity distributors. They opined that this would be counter to the principle of cost causality. Natural gas distributors also noted that the current service charges continue to closely track costs incurred to provide the services. It was however noted that there is commonality in terms of the costs related to issuing notice of switch letters between natural gas and electricity distributors.

Working group energy retailers said that it would be administratively burdensome to have different charges applied by each electricity distributor.

Working group members discussed whether the charges for the notice of switch letter could be the same for electricity and natural gas distributors. There was general agreement from all working group members that the charge should be the same for both electricity and natural gas distributors given that the nature of costs incurred are similar.

Stakeholder Comments on the Draft Report

There were no objections to the OEB's approach to maintain default province-wide electricity RSCs, while maintaining the status quo of distributor-specific charges for natural gas distributors. As well, there were no objections to the approach of establishing a single notice of switch letter charge for both electricity and natural gas distributors.

The OEB's Approach

The OEB will not establish distributor-specific charges for each electricity distributor. The OEB is of the view that this would be administratively burdensome for both electricity distributors and electricity retailers, therefore, default charges continue to be appropriate. As is currently the case, electricity distributors will continue to have the ability to apply for a distributor-specific rate at the time of rebasing.

Given that there are operational differences that exist between the electricity and natural gas sectors, the OEB is of the view that standardization of energy retailer service charges between electricity and natural gas distributors is not warranted. For example, because natural gas distributors have a gas supply procurement function, the nature of the services provided to energy retailers are different than the electricity sector.

The OEB is also of the view that default values for natural gas distributors are not necessary, nor are they required to be updated at this time. This review determined that the charges for natural gas distributors continue to closely track costs and are reviewed, and updated if required, by the natural gas distributors at rebasing.

The OEB will establish a single default charge for electricity and natural gas distributors for the notice of switch letter given that the nature of the services and types of costs incurred are similar between electricity and natural gas distributors.

C. Costing Methodology and Cost Elements

Description

The working group discussed an appropriate costing methodology, the types of costs incurred to provide these services and whether those costs are fixed, variable or semi-variable.

A fully allocated costing methodology was the approach preferred by electricity and natural gas distributors. Most energy retailers suggested that only variable costs be borne by energy retailers. Energy retailers commented that the level of the energy RSCs should allow the retail market in Ontario to be sustained, and that any increase to the energy RSCs should not effectively eliminate the retail market.

Table 3 below shows a summary of the costs identified by Hydro One, which were indicative of the types of costs incurred by the majority of working group members. A more detailed cost matrix can be found in Appendix B.

Table 4: Cost Matrix – Hydro One Networks Inc.

	Fixed	Variable	Semi-Variable
Customer Service Organization		X	
IT Application	X		
Application Support		X	
Finance	X		
Collections – Write off		X	

For both electricity and natural gas distributors, fixed costs identified by the working group distributor members included labour for IT testing and billing personnel that perform the settlement and invoicing of transactions. Variable costs included call center costs and application support. Variable costs were driven by the number of retail customers or the number of transactions. Differences between electricity and natural gas distributors' cost elements were also identified. For instance, natural gas distributors include the costs of commodity related bad debt and system costs in their charges while electricity distributors do not.

Working group electricity distributors submitted data on total costs incurred for providing services to energy retailers. Electricity distributors were also asked to provide an estimate of bad debt attributable to the commodity portion of the bill. Total costs were classified into fixed and variable costs, using the Hydro One cost matrix. While there was general consensus on which cost element was fixed, variable or semi-variable, the level of costs incurred for each of those categories varied significantly across distributors.

Stakeholder Comments on the Draft Report

One retailer disagreed with the inclusion of fixed costs and the use of a fully-allocated costing methodology, noting that the inclusion of fixed costs, which would be incurred by electricity distributors regardless, would not reflect the guiding principle of fairness.

The OEB's Approach

The OEB continues to be of the view that a fully allocated costing methodology is appropriate as it reflects cost causality and value to customers, and would minimize cross-subsidization between ratepayers and energy retailers. Using the approach suggested by one retailer would still result in an increase to the existing electricity RSCs of approximately 90%. This is because the majority of costs identified by the working group electricity distributors are variable.

The OEB agrees that the cost elements identified by the working group distributor members are reasonable. However, for electricity distributors, the OEB believes that the electricity RSCs should also incorporate commodity related bad debt as the risk of default on payment can be directly linked with the service provided to electricity retailers. Section 4A provides further information on this cost element. Section 4A also describes the OEB's final approach with respect to the updated electricity RSCs.

D. Adjustment Mechanism

Description

Working group electricity distributors agreed with an annual adjustment to the charges to keep them up to date and generally supported using the annual adjustment factor applied in the OEB's incentive regulation mechanism (i.e., inflation minus a productivity factor). Natural gas distributors indicated that there was no need to change the current approach used for setting rates, as charges are reviewed at rebasing. The working group also discussed the OEB's approach to adjust the pole attachment charge for electricity distributors. At the time, the OEB had not issued its final report but there was consensus that the same adjustment mechanism to be determined in the pole attachment charge consultation should apply to electricity RSCs. There was support from one working group energy retailer for an annual adjustment mechanism. Another energy retailer said that creating an adjustment mechanism could be cumbersome and suggested that the OEB consider a global review using standard cost allocations for all distributors.

Stakeholder Comments on the Draft Report

Electricity distributors generally supported an annual inflation adjustment to the electricity RSCs. One energy retailer indicated that it also supported the annual inflation adjustment but not the immediate increase of the electricity RSCs as the starting point.

Of the two natural gas distributors who filed comments, only Enbridge Gas asked for a slightly different approach given that some of its energy RSCs are structured as non-utility services and agreements. Enbridge Gas therefore requested that its Agent Billing and Collection charges[5] be excluded from the annual inflation adjustment.

The OEB's Approach

The OEB will implement an annual adjustment based on the OEB's inflation factor commencing on January 1, 2020. The OEB will use the same approach that will be used to implement the adjustment factor for the OEB's pole attachment charge. The OEB is of the view that an annual adjustment similar to the final policy for the OEB's pole attachment charge which is based on inflation (with no offset for productivity) should apply in order to ensure that the charges are kept up to date over time. The OEB is also of the view that this annual adjustment should apply to both natural gas and electricity distributors. The OEB notes that with the implementation of an annual adjustment to the energy RSCs to account for inflation, the differences between revenues and actual costs should be minimized over time.

The annual adjustment for the natural gas distributors' service charges will be accommodated within the new rate-setting framework for Enbridge Gas and Union Gas.[6] The OEB will however exclude Enbridge Gas' Agent Billing and Collection charges given that they are structured as a non-utility service.

Further details on how the annual adjustment will be implemented are provided in Section 5.

[5] Enbridge Gas' Agent Billing and Collection charges are identified in Table 2 of this Report (Category 2 and Category 3).

[6] EB-2017-0306/EB-2017-0307.

E. Electricity Distributor Retail Service Cost Variance Accounts

Description

RCVAs are used to record the difference in revenues and direct incremental costs incurred to provide services to energy retailers. Given the potential for an annual adjustment mechanism to keep the electricity RSCs current, the working group discussed whether this mechanism would negate the need for electricity distributors to continue to use the RCVAs.

Working group members were generally of the view that if the charges were kept updated through an annual adjustment mechanism, the need for the RCVAs would be diminished. However, some members of the working group were of the view that the RCVAs should be kept in place until such time that the electricity RSCs are re-calibrated, as electricity distributors would not have an opportunity to adjust the electricity RSCs prior to rebasing.

The Draft Report proposed the elimination of the RCVAs and the establishment of a new variance account for all electricity distributors. The purpose of the new variance account is to capture the incremental revenues that are a result of the increase in the electricity RSCs in the midst of an incentive rate-setting term, resulting in revenues earned being greater than amounts previously approved in an electricity distributor's distribution rates. The balance in the new variance account would be refunded to ratepayers in a future rate application, and the new account subsequently closed.

Stakeholder Comments on the Draft Report

Electricity distributors did not support the immediate elimination of the RCVAs. Some electricity distributors were not opposed to their eventual elimination but indicated that an immediate elimination could financially disadvantage some electricity distributors.

One stakeholder did not support the elimination of the RCVAs for all electricity distributors. It was opined that the elimination of the RCVAs should be at the discretion of each electricity distributor. This party also did not support the establishment of a new variance account. It was instead suggested that the OEB redesign the existing RCVAs to track both incremental costs and revenues.

Another party recommended that the existing RCVAs be maintained to track the incremental revenues in place of a new variance account. Electricity distributors that no longer use the current RCVAs would be required to use the new variance account.

Some parties also raised difficulties with having to track revenues by rate class as proposed by the Draft Report. It was noted that some electricity distributors may have difficulty tracking revenues by rate class because the revenue transactions relate to electricity retailers rather than retailer customers. It was suggested that incremental revenue could be allocated in the same manner as existing RCVAs, or that incremental revenue could be allocated based on forecasted retail customers.

The OEB's Approach

The comments received confirmed that electricity distributors use two different accounting methods with respect to revenues and costs associated with the provision of retail services. For electricity distributors who currently use the RCVAs, the deficiency or surplus is recorded in the RCVAs, and is eventually collected from or refunded to ratepayers. For those electricity distributors that do not use the RCVA's, the difference between forecast costs and revenues is embedded into their revenue requirement. The two methods are shown in the illustrative example in Table 5 below.

Table 5: Accounting Methods - No RCVAs vs Using RCVAs

METHOD 1 **Electricity Distributors who no longer use the RCVAs**	**METHOD 2** **Electricity Distributors who currently use the RCVAs**
Base Distribution Rates: - OM&A includes $1,000 - Other Revenue Offsets include $800	Base Distribution Rates: - OM&A excludes $1,000 - Other Revenue Offsets exclude $800
Revenue Requirement: Includes $200 in deficiency from retail service costs/revenues	Revenue Requirement: Unaffected by retail service costs/revenues.
Accounting Method: No RCVAs accounting entries required.	Accounting Method: RCVAs used to collect/return $200 difference in cost/revenue.

Note: The illustrative example in this table assumes the following: 1) forecasted costs associated with retail services are $1,000 and 2) forecasted revenue from electricity RSCs is $800.

As indicated in the Draft Report, there are two electricity distributors[7] who have recently been granted OEB approval to no longer use the RCVAs and there are also many electricity distributors who no longer track the revenues and costs for retail services in the RCVAs.

Given the concerns raised by electricity distributors regarding the immediate elimination of the RCVAs, the OEB has determined that an immediate elimination of the RCVAs for

[7] Toronto Hydro-Electric System Limited (EB-2014-0116) and Hydro Ottawa Limited (EB-2015-0004).

all electricity distributors is not warranted. The OEB continues to believe that, for those electricity distributors that are currently using the RCVAs, the elimination of the RCVAs is appropriate but will allow for this to occur at rebasing along with final disposition of the balances in the RCVAs. Electricity distributors with a longer deferral period prior to rebasing can ask for disposition of the RCVAs prior to rebasing if the amounts in the RCVA are significant, however, the RCVAs will remain open until rebasing. The OEB does not see merit in electricity distributors continuing to track these variances any further past rebasing. Following rebasing, those distributors are expected to include in their revenue requirement the difference between forecast costs and revenues associated with retail services. Electricity distributors still using the RCVAs shall continue to track the balances in accordance with the guidance set out in the OEB's *Accounting Procedures Handbook for Electricity Distributors*.

The RCVAs were established at market opening when electricity distributors first began to settle with electricity retailers. At that time, there was uncertainty about the cost of the settlement process and the RCVAs tracked the costs and revenues to enable an evaluation of the appropriateness of the approved rates at a later date.[8] Settlement with electricity retailers has now been an integral part of the operations of electricity distributors for more than 16 years. The OEB considers that activities relating to the settlement with electricity retailers are now part of ordinary business for distributors and therefore the OEB does not see merit in a regular true-up of these costs.

The OEB will proceed with the establishment of the new variance account. The new variance account will capture incremental revenues, but only for those electricity distributors that no longer use the RCVAs.

The balance in this new account will be disposed of at the electricity distributor's next rebasing application and the variance account will then be closed. Electricity distributors that are in the midst of lengthy deferral periods, have the option of applying for disposition of the account in an incentive rate-setting application if the balance is significant. In this instance, the account will remain open to continue to track amounts until rebasing.

The new variance account will track incremental revenue only, as commodity related bad debt is already included in the distributors' base rates. For administrative ease, the incremental revenue will be allocated on the same basis as the RCVAs (i.e., based on number of customers) as opposed to a direct assignment.

[8] *Accounting Procedures Handbook for Electricity Distributors*, Article 490.

4. NEW ELECTRICITY RETAIL SERVICE CHARGES

This section discusses the OEB's approach for updating electricity RSCs. As previously mentioned, there will be no updates to the current energy retailer service charges for natural gas distributors as they continue to closely track costs. The new service charge for the notice of switch letter will, however, be applicable for both electricity and natural gas distributors.

A. Updates to Current Electricity Retail Service Charges

Description

Working group distributors submitted data on total costs incurred for providing services to energy retailers. Electricity distributors were asked to provide costs from 2016 as it represented the most recent year for which actual year-end data was available. In addition, electricity distributors were asked to provide an approximation of the total annual bad debt for electricity retailer customers for the commodity portion of the bill only. Two of the electricity distributor working group members (London Hydro and Hydro One) provided data on commodity related bad debt, while the others were unable to do so. Total costs were classified into fixed and variable costs, using the cost matrix provided by Hydro One.

As part of the working group discussions, electricity distributors generally agreed that the revenues generated from the electricity RSCs should be doubled. Working group energy retailers did not specifically address the quantum of the increase of the charges in their written comments following the conclusion of the working group meetings, but indicated that any adjustment to the existing electricity RSCs should be substantiated and that a further breakdown of costs from more than the five working group electricity distributors should be provided.

Stakeholder Comments on the Draft Report

Electricity distributors generally agreed that adjusting the electricity RSCs to ensure that the revenues are more closely aligned to the costs is a good initial step to address the current under-recovery that exists, but indicated that the OEB should review the electricity RSCs on a more frequent basis going forward.

One retailer disagreed with the level of adjustment to the electricity RSCs because it is well above an increase to account for inflation since 2002. A 40% increase was recommended instead, or if the OEB was to proceed with the adjustment being proposed, a five year phase-in may be more appropriate. It was noted that an immediate increase in the electricity RSCs would add tens of thousands of dollars to operating costs. Another retailer did not specifically address the proposed adjustment of the electricity RSCs, but indicated its disagreement with the use of a fully allocated costing methodology which includes the recovery of fixed costs.

The OEB's Approach

The OEB continues to be of the view that adjusting the electricity RSCs to address the under-recovery and to eliminate the cross-subsidization that currently exists in a timely fashion is appropriate. Currently, revenues collected from retailers cover about less than half the costs incurred to provide service. The updated electricity RSCs will apply to all electricity distributors.[9]

As discussed in Section 2C, the approach suggested by one retailer would still result in an increase to the existing electricity RSCs of approximately 90% because the majority of costs identified by the electricity distributors in the working group are variable. The OEB does not see merit in phasing in the level of the electricity RSCs given there have been no changes since 2002 resulting in a large cross-subsidization built up over time. The OEB is of the view that it is not in the public interest to continue that cross subsidization, even at declining levels over the next five years, as suggested by a retailer.

Based on the data provided by working group electricity distributors, a total under-recovery of approximately $1.6 million was identified for the last full year for which this data was available (2016). This under-recovery represents approximately 60% of the total costs incurred to provide services to electricity retailers and includes estimated commodity related bad debt for two of the five working group electricity distributors (London Hydro and Hydro One).[10] A breakdown of expenses and revenue by working group electricity distributor is provided in Appendix C.

The OEB agrees with the electricity distributor working group members that it is an appropriate time to adjust the electricity RSCs to ensure that revenues recovered from retailers are more closely aligned with the costs of providing service. While doubling the electricity RSCs does not fully eliminate the total revenue deficiency identified by electricity working group members, the OEB is of the view that this level is appropriate. With respect to the data used by the OEB, the OEB is of the view that the sample size is

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[9] Hydro Ottawa's electricity RSCs have been adjusted by an inflationary rate since 2016. The updated electricity RSCs will also apply to Hydro Ottawa.

[10] The other three working group electricity distributors were unable to provide this data.

sufficient as the five electricity distributors collectively serve approximately 40% of customers in Ontario.

While the OEB intended, to the extent possible, that the new electricity RSCs reflect the nature of the costs (fixed vs. variable) incurred to provide service, analysis of the data provided by electricity distributors revealed wide variability in the level of fixed and variable costs. As a result, the OEB used a top-down approach in determining electricity RSCs, excluding the Retailer Service Agreement charge, to be consistent with the approximate level of the overall cost under-recovery. The Retailer Service Agreement charge is a one-time charge incurred when an electricity retailer establishes a service agreement with an electricity distributor. Most working group members were of the view that the current level is reflective of costs incurred to provide that service.

Altogether, the OEB is of the view that the new electricity RSCs reasonably reflect the principles established by the working group. The OEB will implement the updated electricity RSCs in 2019. The electricity RSCs will be adjusted for inflation annually commencing on January 1, 2020. The updated electricity RSCs for implementation are shown in Table 6 below.

Table 6: Current and New Electricity Retail Service Charges

Category	RSCs	Unit	Current Charges	New Charges	Description
1. Establishing Service Agreements	Retailer Service Agreement	per agreement (one-time)	$100.00	**No Change**	Intended to cover costs related to the service agreement between an electricity distributor and electricity retailer
	Monthly Fixed Charge	per retailer (monthly)	$20.00	**$40.00**	
	Monthly Variable Charge	per retail customer (monthly)	$0.50	**$1.00**	
2. Billing	Distributor Consolidated Billing Charge	per retail customer (monthly)	$0.30	**$0.60**	Intended to recover the incremental costs for an electricity distributor to provide distributor-consolidated billing. A credit is paid to electricity retailers that choose retailer-consolidated billing.
	Retailer Consolidated Billing Credit	per retail customer (monthly)	$(0.30)	**$(0.60)**	
3. Service Transaction Requests	Service Transaction - Request fee	per request	$0.25	**$0.50**	Intended to recover the incremental costs of labour, internal information system maintenance costs, and delivery costs.
	Service Transaction - Process fee	per request	$0.50	**$1.00**	
	Information Standard Delivery Charge	per request, after 2 free requests	$2.00	**$4.00**	

B. Notice of Switch Letter Service Charge

Description

The data submitted by electricity distributors working group members showed that the costs to issue the notice of switch letter ranged between $1.00 and $3.00. For the two natural gas distributors, the costs were $1.17 and $1.67 respectively. Electricity and natural gas distributors indicated that they incur costs for postage, paper, envelope, printing, and call handling for the notice of switch letters. The average cost for all working group distributor members is $1.91 per notice of switch letter. The OEB understands that the working group members are sending letters by standard mail for the most part, although the Retail Settlement Code does allow for other means to send the letter such as by email.

One working group energy retailer indicated that it was sending a letter similar to the OEB's notice of switch letter prior to it being mandated as of July 1, 2017, and its cost per letter was $1.07, excluding labour, which is less than the estimated costs of some members of the working group.

Stakeholder Comments on the Draft Report

Electricity distributors generally supported the establishment of a new service charge of $2.00, but indicated that the service charge should be optional. Electricity distributors indicated that that costs to implement the new charge might exceed the $2.00 charge per letter.

Just Energy suggested that the OEB consider a charge of less than $2.00 given the lower costs of the two natural gas distributors compared to the working group electricity distributors. Just Energy also questioned whether the OEB considered allowing the energy retailers to send the notice of switch letter directly to customers to achieve lower costs.

The OEB's Approach

The OEB will establish a new notice of switch letter service charge for both electricity and natural gas distributors of $2.00, which is the rounded average to the closest dollar of the costs provided by working group distributors. The OEB acknowledges that this charge is higher than the costs identified by one energy retailer, but notes that the $1.07 figure is exclusive of labour costs and therefore would not include call handling costs. Based on the principle of cost causality, the OEB is of the view that including call handling costs is appropriate. The new service charge will apply to letters sent by standard mail only given that the costs provided by working group distributors are generally related to sending the letters by standard mail. The OEB has also determined that the adjustment factor discussed in Section 3D will apply to the new service charge. The new service charge will be implemented in 2019.

Some comments suggested that electricity and natural gas distributors should have the option to apply the new charge to an energy retailer when issuing a notice of switch letter. The OEB agrees that electricity and natural gas distributors should have the option to opt out of charging energy retailers the new $2.00 service charge when mailing the Notice of Switch Letter, if the costs (e.g., system changes) outweigh the benefits. The opt out only applies to the application of the $2.00 charge and does not negate the requirement under the Retail Settlement Code and the Gas Distribution Access Rule requiring electricity and natural gas distributors to send a written notice to any low volume consumer who has signed a contract with an energy retailer. The OEB believes that this change in approach will especially benefit electricity distributors with low energy retailer customer numbers and who typically send fewer letters in comparison to larger electricity distributors who have a greater proportion of energy retailer customers.

Electricity and natural gas distributors that choose to opt out of applying the $2.00 charge will be required to file a one-time letter with the OEB to indicate their intention to opt out 60 days after the issuance of any final rate order that follows this consultation. The OEB expects that electricity and natural gas distributors that have opted out will notify the OEB when filing an incentive rate-setting or cost based application should they decide to commence applying the charge.

5. IMPLEMENTATION

The OEB will implement the updated electricity RSCs in 2019. The OEB is issuing a draft rate and accounting order for stakeholder comment. The draft order contemplates an effective date of May 1, 2019. The new service charge for the notice of switch letter will also come into effect on this same date.

The annual inflationary adjustment mechanism for the energy retailer service charges for electricity and natural gas distributors will take effect on January 1, 2020. For electricity distributors, the OEB will use the same process that it will follow to implement the annual adjustment for the pole attachment charge. To that end, the OEB will update the generic charges annually and not rely on utilities bringing forth proposals in their annual rate applications.

As indicated in the Draft Report, the OEB will issue a generic order every December to adjust all miscellaneous service charges that are subject to an inflationary adjustment to be effective January 1st of each year. The OEB acknowledges the comments from one stakeholder that confirmation of the annual inflation factor prior to November 1st would facilitate accurate rates and implementation for electricity distributors. The OEB will determine the exact date of the inflationary adjustment order on a year by year basis. Natural gas distributors will update their charges on a distributor-specific basis as part of their annual rates applications.

The OEB also acknowledges that in order to facilitate changes to customer information systems and Electronic Business Transactions (EBT) standards (which will require internal and external resources and testing), implementation should occur at minimum three months after issuance of this Report. The OEB confirms that the application of the new charges will be prospective. As discussed in Section 4B, electricity and natural gas distributors will be allowed to opt out of charging for the notice of switch letter if the costs outweigh the benefits. For the new notice of switch letter charge, electricity and natural gas distributors who do not opt out of sending it will be able to use a currently unused charge type (that should be re-named), negating the need to incur additional costs of having to add a new charge in the EBT system.

APPENDIX A

WORKING GROUP TOPICS LIST

	Topic
1.	The overarching guiding principles that the OEB should consider.
2.	The type of costs that should be included as part of the overarching costing methodology for distributor-consolidated billing, service transaction requests, service agreements, and notice of switch letters.
3.	Whether a fully allocated costing methodology is appropriate for existing energy retailer service charges and if not, the other approaches that the OEB should consider.
4.	Whether a consistent application of energy retailer service charges should be followed or whether distributor specific charges should apply.
5.	Whether a mechanism should be considered by the OEB in order to keep energy retailer service charges up to date.
6.	Whether Retail Service Cost Variance Accounts (which are used to record the difference between charges levied on customers and retailers and the direct incremental costs for the provision of retailer services) should be eliminated and the implications of doing so.
7.	Whether there are approaches or lessons learned for charges from the natural gas distributors to natural gas marketers that could be considered for electricity and vice versa.
8.	The factors that the OEB should consider with respect to the implementation of any changes made to the current energy retailer service charges.

APPENDIX B

HYDRO ONE COST MATRIX

	Fixed	Variable	Semi-Variable
Customer Service Organization			
Retailer emails/communication/Account analysis/Offline settlements/Summary Billing/Net Metering		X	
Call Centre - Retailer specific call handling		X	
(Settlements) Process Retailer Enrolled Complex Billed Accounts		X	
IT Application			
Internal Application Costs (system maintenance/upgrades)	X		
spi/ERTH	X		
Application Support			
Retailer Issues, EBT Exceptions and Tickets		X	
Integration (iHUB and PI) monthly support		X	
Finance			
Invoice Settlement Total (IST) Payable/Receivable Reconciliation	X		
Invoice Bill Ready (IBR) Payable/Receivable Analysis	X		
Reporting & Analysis	X		
Collections - Write off			
Total Retailer Charges Written Off		X	

APPENDIX C

ELECTRICITY DISTRIBUTOR RETAIL SERVICES EXPENSES AND REVENUES

Electricity Distributor	Total Expenses A	Total Revenue B	Total Under-Recovery C = A - B
Guelph Hydro	$ 91,000	$ 22,753	$ 68,247
Hydro One	$ 1,539,000[1]	$ 619,658	$ 919,342
Hydro Ottawa	$ 559,086	$ 177,364	$ 381,722
London Hydro	$ 182,801[2]	$ 73,161	$ 109,640
Veridian Connections	$ 221,838	$ 83,821	$ 138,017
Total	**$ 2,593,725**	**$ 976,757**	**$ 1,616,968**

Notes:
[1] Includes an estimate of commodity related bad debt of $78,000.
[2] Includes an estimate of commodity related bad debt of $47,784.