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MANUFACTURERS
& EXPORTERS



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DU CANADA

January 25, 2019

Ms. Rosemarie T. LeClair
Chair & Chief Executive Officer
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Re: Advisory Committee on Innovation

Dear Ms. LeClair,

On behalf of our 2,500 direct members at Canadian Manufacturers & Exporters (CME), the tens of thousands of manufacturers across Ontario and the nearly 780,000 employees, we appreciate the opportunity to provide comments to the Ontario Energy Board on the Advisory Report on Innovation which is of great interest to our members.

Our submission can be found attached below. Please contact us if you have any questions or require additional information.

Sincerely,

A handwritten signature in black ink, appearing to read 'A. Greco'.

Alex Greco
Director, Manufacturing Policy

Executive Summary:

Canadian Manufacturers & Exporters (CME) acknowledges that a report has been commissioned by the Advisory Panel on Innovation. We appreciate the OEB's continued efforts to deliver an efficient regulatory system and its efforts to protect ratepayers. However, we believe based on this report that significant improvements must be implemented to ensure fairness, accountability, consumer protection, and transparency for ratepayers across Ontario. CME believes that the ratepayers' interests need to be protected so that regulated entities can be obligated to report on their efficiency, new costs, benefits and corresponding impacts. The OEB should encourage innovation, while being mindful of consumers and the affordability of electricity rates to encourage economic growth and development; particularly for the manufacturing sector which continues to be the most critical engine of the Ontario economy. The manufacturing sector must be supported in providing their inputs through the collective efforts of industry and experts retain to level the playing field.

Based on the collective concerns of our membership, CME's recommendations are as follows:

1. The OEB must reinforce its role in protecting ratepayers based on outcomes and evidence-based objectives and also account for the competitiveness of Ontario's economy.
2. A new stakeholder forum must be established to ensure full representation from all stakeholders, including manufacturers.
3. Related initiatives should be merged into a single exercise in order to guard against competing "innovation forums" and to provide a comprehensive path forward.
4. The OEB needs a new mechanism to address the total system cost in business cases and should be under one system.
5. The OEB must clearly define what goes into its category of "regulated base".
6. A clear definition of what is considered "innovation" under the OEB's mandate must be established.

About Canadian Manufacturers & Exporters (CME)

Since 1871, CME has been fighting for the future of Canada's manufacturing and exporting communities and helping them grow. The association directly represents more than 2,500 leading companies nationwide. More than 85 per cent of CME's members are small and medium-sized enterprises. As Canada's leading business network, CME, through various initiatives including the establishment of the Canadian Manufacturing Coalition, touches more than 100,000 companies from coast to coast, engaged in manufacturing, global business and service-related industries. CME's membership network accounts for an estimated 82 per cent of total manufacturing production and 90 per cent of Canada's exports.

Background/Context

Ontario's electricity system is complicated with many moving parts. As we have seen over the last few years, there have been many articles, discussions and consultations on "innovation" in the electricity sector. "Distributed Energy Resources", "Microgrids" and "Prosumer" are all terms that have been apparent in the stakeholder engagement process and have been used to format what tomorrow's electricity systems will look like for Ontario's manufacturing sector. The transition will be exciting and will feature radically different paradigms regarding the use and supply of energy in the province. While intriguing and mindful that we must look towards the future, we need to be mindful

of cost associated with “innovation”. It was CME’s intention throughout this consultation that since this Advisory Committee was initiated by the OEB itself, that it would have an appropriate cost and customer focus, or at least consider it as a conduit to key elements related to innovation. Unfortunately, in our view this does not appear to be the case.

According to the OEB, the mandate of the committee is as follows: “the Committee will focus on identifying actions that a regulator can take to support and enable cost effective innovation, grid modernization, and consumer choice to help inform regulatory policy development.” Whether the problem is with the charge itself or with its interpretation by the Committee is irrelevant. What is relevant is the direction endorsed by the Committee, a direction that appears to focus on reducing the regulatory burden for utilities and allowing utilities to better compete in innovated products and services. The report includes such specific recommendations as:

- Relax elements of the Affiliate Relationships Code (1D)
- Strong consideration of utility remuneration to keep them whole (2A)
- Significant focus on DER project proponents and their ability to be appropriately compensated (2C)
- Significant emphasis placed on reduction of oversight (4A, 4B, 4C, 4D), and, regulatory reviews and timelines are to be streamlined and shorter (4C, 4D) even though risk associated with Innovation is going to be higher (2D)
- Provision of additional funding to utilities to facilitate innovation (2D)

CME believes that these recommendations appear somewhat prejudiced toward the utility view. To be clear, we believe utilities play a significant role in the electricity system and they need to continue to play such a role. However, there is little evidence of the consideration of the ratepayer perspective nor does there appear to be any meaningful focus on affordability and what innovation can do to improve this. This is a significant flaw in the report and as a result it requires us to have the position that a review of the goal of this consultation process, requiring a fundamental review of the goal of this exercise.

Key issues with the report

CME believes there are the following five concerns in the report that need to be highlighted. One is with respect to the Committee itself and one is with respect to the Committee’s analysis and findings:

Composition of the Committee

With no disrespect intended to the current Committee Members, this Committee has no manufacturing/customer representation at all with the exception that the Terms of Reference document specifically calls out “representation from ... consumer interests”. Instead, the committee appears to be generally comprised of utilities and consultants. The committee in our view needs balanced representation to ensure appropriate customer/manufacturing representation and to help ensure the best outcomes for ratepayers.

The Issue of Stranded Costs

All references to costs by the Committee in its Report are on a going forward basis only. There is no consideration of the potential for stranded costs to occur as a result of the move towards innovation in the energy sector. This is a significant omission and requires further elaboration. As a result of “innovation”, the potential for stranded costs associated with a grid defection approach is very high. Yesterday's electricity system relied on a centralized model for planning and operation. It evolved that way due to the desire to achieve economies of scale and the need for improved reliability. It seemed reasonable to only have one major system, since it was so capital intensive to build it. Almost all the innovation discussions taking place now regarding tomorrow's system revolve around a somewhat different theme - decentralization or, “grid defection” with the idea being that we can maintain the benefits of a centralized system, while enjoying the new-found products and choices that will exist in an innovated world. It's important at this point to remember what it is that is driving this grid defection. It is not dissatisfaction with reliability, nor is it an unquenchable thirst for the novel; it is quite simply, the cost of electricity.

The big problem here is the transition between these two worlds. We already have the old-world system. And we continue to pay for that every time manufacturers pay electricity bills – costs that are already too high. Utility infrastructure in the province is worth tens of billions of dollars – generally included within utility rate base. That rate base is paid for by all consumers on an ongoing basis. Many of the forms of innovation being discussed provide incentives to reduce reliance on the existing grid. Reduced reliance will lead to the perception of reduced responsibility for the costs of that centralized system. Those costs still need to be paid - but fewer and fewer people will feel obligated to do so. That's how stranded costs will be created. We need to understand this unintended effect and neutralize it before we end up with costs that could make current Global Adjustment charges look small, by comparison. This Committee has ignored that concern, instead focusing on the need for regulatory reform, and the safeguarding of future utility revenues.

Comments on Regulatory Issues

CME has several concerns with respect to the regulatory issues that are referenced in the report. They are described in more detail in alignment with certain sections of the report.

Section 2B

Section 2B of the report provides an example of an instance where, in the Committee's view, the regulatory process impedes innovation - the investment in batteries as opposed to a distribution line. No one would argue with the fact that ratepayers would prefer the battery if we knew that the distribution line would be stranded, but the utilities put significant work into forecasting demand, if they can provide no evidence in advance for a lessening in demand, why should the optionality be valued highly, if at all? Challenging benefits such as optionality through the regulatory process ensures that there is objective and tested evidence supporting optionality as a benefit under the specific investment circumstances of the application, rather than taking as a benefit *a priori*.

Section 2B also states that “Establishing a common evaluation method that accounts for all benefits associated with any particular solution” will help provide “regulatory predictability” since utilities would “not have to justify the benefits included in their business case and how they were determined”. In CME's view, utilities should have to justify what benefits are included in their

business cases and how they were determined before the OEB. To the extent that these benefits are tested by the Board and found to be methodologically sound, those benefits and methodologies become normalized, and may face fewer challenges in the future. What is critical is that ratepayers, who ultimately bear the costs of innovation, and the Board, charged with protecting consumer interests, are allowed to comprehensively test them *before* they are accepted.

Moreover, the report establishes an empirical evaluation methodology for cost-benefit comparison. The first paragraph of this section states that “one of the reasons utilities may not pursue innovative solutions is that developing a business case and defending it before the regulator and intervenors is more challenging” than continuing with the status quo. While we agree with this sentiment, CME submits that that is the natural and desirable state for regulation to be in. Regulators and advocates for ratepayers should challenge new ideas more rigorously. There is no question that there are good innovative ideas that are or could be put forward, there are also ideas which should be rejected as not being in the ratepayers’ interest. Making sure that the utility has done its due diligence and is not moving forward with an idea immediately, the failure of which is ultimately borne by the ratepayers, is central to CME’s role as an intervenor. CME is of the mind that the solution isn’t to change the rigor of regulatory scrutiny but to get better or more thought out ideas.

Section 4C

In Section 4C, the report recommends exploring the use of self-executing processes. Under the self-executing process, proposals selected and planned in accordance with prescribed criteria would require no further regulatory approval to proceed, and “[a]ny after-the-fact review of utility performance would focus on learning from experience in the interests of continuous improvement rather than on a hindsight critique of what a utility could have done differently.”

CME interprets this to mean that the utilities want to plan their proposals in accordance with a formula and submit it to the OEB without giving due regard to the specific circumstances of each application. CME submits that this is distinctly averse to the interests of ratepayers.

Under this paradigm, if the proposed project were to go over budget and behind schedule, the utilities would conduct a ‘lessons learned’ review. To be clear, CME respects this process and believes that ‘lessons learned’ reviews can be helpful. That said, it brings into question about what protection there is for ratepayers. There is always the risk that the project may not be run appropriately. CME submits that utilities should continue to be held accountable for those failures. To the extent that a utility could have done things differently, they should be critiqued on that basis. “Lessons learned” may be insufficient to prevent the same problems from recurring on other proposals, and accordingly a hindsight critique continue to be in ratepayers’ interests.

Innovation Sandbox

We acknowledge that the OEB is moving ahead with this aspect of the report. However, this has been done without consultations with manufacturers. While this may appear reasonable in a world where innovation is generally regarded as a positive step forward, the details of the Sandbox process must be fully considered.

Section 4a) paragraph 1 states the following about the report: “The complexity of utility filings and the adversarial nature of OEB hearings may be an obstacle to innovation and experimentation by consumers, utilities and innovators.” In CME’s view, if the adversarial process exposes the idea as a poorly thought out one, and rejects it on that basis, isn’t that a value of the process, not a detriment? This section of the report articulates the notion that a sandbox is intended to balance innovation and reducing the regulatory burden. While CME supports that goal, we submit that it would be in the best interest for manufacturers and ratepayers to just have a simplified, fulsome and rigorous process to weed out costly or sub-standard innovation ideas.

While there is no direct statement on the OEB website that conversations between utilities and OEB staff will be confidential, the following language is used to describe the interactions “An informal and open dialogue between innovators and OEB staff may be used...”. This suggests that the conversations will not be made public, which was the impression that CME had from the consultation session.

When the points above are considered, it becomes apparent that the process in question will be conducted without public knowledge or input, with the outcome not having benefitted from a public hearing process, and with the exemptions being granted potentially including statutory provisions. For a quasi-judicial tribunal whose objectives under the Ontario Energy Board Act include protecting the interests of the consumer, this seems unnecessarily mysterious. It certainly does not seem to support an open and transparent approach to business. The Board’s imposition of this, with no opportunity for discussion prior to its implementation, appears inconsistent with the consumer focus that exists in numerous OEB documents including, but not limited to, its Business Plan, its Handbook to Utility Rate Applications and its Strategic Blueprint itself. CME finds the Sandbox as well as how it was introduced, to be a step backward in terms of inclusiveness and transparency. In our view, policies and practices that spur innovation need to be implemented to ensure Ontario’s energy infrastructure is modernized and affordable and both the manufacturing and energy sectors are set up for success. At the same time, it is critical for ratepayers and the sustainability of the manufacturing sector itself that the OEB not create barriers for stakeholders to enter the market. Manufacturers/ratepayers cannot be seen to be bearing the costs of doing business in Ontario.

Recommendations:

Based on the collective concerns of our membership, CME’s recommendations are as follows:

1. **The OEB must reinforce its role in protecting ratepayers based on outcomes and evidence-based objectives and also account for the competitiveness of Ontario’s economy.** OEB needs to consider the competitiveness of the economy when making rate rulings. It should also focus on timely decisions as to how the OEB can best address energy sector evolution using existing regulatory powers and tools, including setting rates. At the same time, the OEB’s mandate needs to lower electricity costs for the benefit of Ontario’s manufacturers by directly reducing electricity bills.

2. **A new stakeholder forum must be established to ensure full representation from all stakeholders, including manufacturers.** The engagement should be externally facilitated, and its scope should be broader than the scope used by the current Advisory Committee.
3. **Related initiatives should be merged into a single exercise in order to guard against competing “innovation forums” and to provide a comprehensive path forward.** Only after this process is concluded, can a discussion of potential regulatory reforms to enable innovation (while preventing stranded costs) take place. Even then, strict objectives for those reforms must be established up front objectives that not only consider the financial viability of the regulated utilities, but also reflect consumer needs and economic realities.
4. **The OEB needs a new mechanism to address the total system cost in business cases and should be under one system.** The current challenge is many cost elements are not currently regulated by the board. And the notion of “lowest cost” is not emphasized in the report. In CME’s view, lowest cost is not the same as cost effective. Innovation can help lower electricity rates, but it must do so while keeping in mind the ratepayer and the need to lower electricity rates for ratepayers.
5. **The OEB must clearly define what goes into its category of “regulated base”.** CME believes that we need to protect the captive customers within the rate base. Moreover, early adopters need to be encouraged on a commercial basis to adopt innovation within their energy systems through pilot projects and other means. However, this must be done in such a way where there can not be any cost transfer of commercial efforts into the rate base.
6. **A clear definition of what is considered “innovation” must be established under the OEB’s mandate.** A framework of requirements that innovations are trying to solve needs to be established so that ratepayers have the best opportunity to bring down electricity costs. As such, there must be a clear definition as to what the innovation agenda is trying to solve.

CME would be pleased to discuss with the OEB our consultation response more in detail.

Contact Information:

If you would like more information about the content of our response, please contact:

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