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By EMAIL and RESS

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Ontario Energy Board
2300 Yonge Street
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Attn: Nancy Marconi, Registrar

Dear Ms. Marconi:

Re: EB-2021-0118 – Framework for Energy Innovation – SEC Submissions

We are counsel for the School Energy Coalition. Further to the OEB's letter of July 6, 2022, this letter constitutes SEC's submissions on the Report of the FEIWG and the related Subgroup Reports (collectively the "Report").

The undersigned was a member of FEIWG, and had extensive input into the Report. We will seek as much as possible to avoid reiterating that input here. These submissions respond to the six further questions posed by the OEB in its July 6th letter.

1. What is the relative priority of the issues and next steps identified by the FEIWG?

This General question should be disaggregated into two questions, which are conceptually distinct.

Reimagining the Sector. The broader question is a rethinking of the paradigm being used for utility remuneration in Ontario. This in turn requires re-examining the scope of the natural monopoly, and therefore the scope of activities that should or could be left to the competitive markets.

As customers get their energy services more and more from a variety of suppliers, many of them competitive, the role of the regulated utility is going to change. At the same time, as those competitive suppliers expand their market share, the return on rate base method of remunerating monopoly franchise holders will increasingly be a barrier to the best results for customers.

The process to consider how, if at all, the monopoly scope and the remuneration paradigm should evolve is a complex one, and is likely to involve both the regulator and the government in a series of steps. In our view, it would benefit the sector if the first steps in rethinking those issues were started now. While the OEB is not likely to get completely ahead of the pace of change, it can increase the chances that it will not be forced into reactive-only policymaking because the competitive markets have moved too fast.

Therefore, it would be useful for the OEB to commence this analysis with an options paper, written by OEB Staff, as a method of inviting input from the sector on how it will, or should, evolve. This should include questioning many of the fundamentals, such as what aspects of the wires (or pipes) business can be competitive, and whether the protected monopoly of distributors should be open to challenge if other providers (even other regulated utilities) can deliver the service cheaper, and whether ROE should be abandoned, or should be modified to be performance-driven. Those are just a few of the examples.

While this would all appear to be very "blue sky" in nature, SEC believes that consultations on the high level issues now will help the OEB make decisions about the day-to-day issues down the line within a commonly-understood context.

Prioritization of Report Recommendations. The narrower approach to the first question is focused on the seven main recommendations in the Report. Many of them, of course, can be carried out in parallel, but a couple should, in our view, be prioritized.

Recommendations 6 and 7 both relate to information, which is in fact a theme throughout the Report. Competitive markets are at their root controlled by information flow. As information flow is improved, more cost-effective DERs will be available to customers and utilities.

SEC believes that an early policy determination promoting transparency is a high priority, with as much information on both DER proposals, and system needs, as utilities can make readily available to the customers, the regulator, and the market. The OEB should consider, not just timely reporting to the OEB on applications, and system constraints, and the like, but also ongoing public disclosure of those facts.

By way of example, it should be possible to go to the website of any distributor and see immediately where on their system there are issues and constraints today, and where they forecast such constraints will arise in the future. As much as possible, this should be real-time information. The more information is available to the market, the more the market can respond with cost-effective solutions.

SEC notes that, of course, the other benefit of mandating increased information flow is that the OEB will have more information on which to base ongoing policy decisions. One noticeable aspect of the FEIWG deliberations was the shared realization that there are many types of information asymmetry, and they can be a barrier to common understanding of the issues.

2. What is the appropriate scope of a BCA Framework? In other words, should a narrow or broad set of benefits and costs be considered with respect to deployment of DERs as alternatives to traditional solutions to meet electricity distribution system needs?

The Report correctly identifies that the BCA Framework will have two purposes: information/ analysis, and decision support.

It is, in our view, self-evident that all costs and benefits should be considered in determining how to best meet the needs of the customers. There is no serious justification for pretending that any material cost, or benefit, just doesn't exist. Why would anyone do that?

On the other hand, when making decisions it is important to consider, not just the value of any cost or benefit (often by itself a non-trivial problem), but also who pays the cost and who receives the benefit. As the Report notes, the BCA Framework will not exist in a vacuum. It will exist within a system in which costs and benefits are somewhat scattered, both in terms of who pays/benefits, and who has jurisdiction to balance those costs or benefits. It also will exist within the context of costs and benefits that are hard to quantify, or are risks/potentials rather than costs and benefits.

Thus, if a distributor makes a decision on a non-wires alternative, and includes all costs and benefits, the result may be that society is better off in total, but distribution rates are higher. Conversely, if a distributor makes that same decision considering only the costs and benefits that can be quantified in distribution rates, often the outcome will not be the best overall outcome for the customers, or some of them.

In our view, a BCA Framework should include all costs and benefits, including even those that cannot be quantified. Relevant information should not be ignored.

On the other hand, the application of that BCA Framework to utility decision-making should not be a mechanistic process. When considering alternatives, all costs and benefits should be reviewed, but a judgment call is required as to the weight given to each in the particular circumstances. That judgment may be different if the nature of the alternative, or the nature of the constraint, is different.

SEC therefore believes that the BCA Framework should not be a spreadsheet model, or other fixed calculation, but should be a process of analysis. It should stipulate what information should be gathered by the utility or the regulator, and can establish rules as to how at least some of the costs and benefits should be valued. The analysis should then consider who benefits, who bears costs, any mismatches that will arise, and any methods available to balance those issues. The goal should be to identify and quantify with clarity all of the impacts of the choice, without necessarily adding them up and getting a "net benefit".

SEC notes that all of the above is rudimentary, because in our view the development of a more rigorous BCA Framework will arise only after the OEB has had an opportunity to consider multiple examples of cost/benefit analyses in detail. SEC would expect there to be multiple iterations over the next several years.

3. How might the OEB remove disincentives for utilities to adopt DER solutions?

Rate of Return Regulation. As noted earlier, a major disincentive is the return on rate base concept, since every choice of a non-wires alternative involves giving up growth in assets and therefore profits. This disincentive cannot be removed easily.

Cost Recovery Uncertainty. A second disincentive, and often more important, is uncertainty of cost recovery. Adopting DER solutions often involves investments (whether they are capital or operating costs) in unique or new circumstances. Faced with the normal uncertainty surrounding uniqueness or innovation, many utilities will opt for the approach they know is acceptable, i.e. the traditional answer. Even if it is ultimately more expensive for the customers, the cost recovery to the utility is not in doubt.

Utility managers are expected to be risk-averse. Uncertainty is something we generally want them to avoid, yet DERs are less likely to happen if no-one is willing to take any risks.

There are process improvements that could be implemented, but none of them really solve this cost recovery question. The only way it can be resolved is for the OEB, and panels of commissioners, to demonstrate over time that a) utilities that take risks to benefit their customers will not be routinely punished for doing so, and b) utilities that stick to traditional approachs rather than looking at new ones will have increased risk that they will not be able to recover their costs.

In the former case, a utility that takes a prudent (at the time) risk to benefit customers should be applauded for doing so, even if it doesn't work out. In the latter case, utilities whose capital and operating plans do not implement any alternatives, and as a result pass on higher costs to customers, should risk disallowance for failing to sufficiently explore non-wires options.

Utility Personnel and Practices. One of the biggest disincentives is the difficulty utility managers with traditional training and experience face in thinking about their system needs differently.

The OEB can ameliorate this issue two ways.

First, the OEB can establish new planning expectations that work from the customers' perspective back to the system requirements, rather than the other way around. The easier approach is to determine the traditional solution to a constraint or need, then see if a non-wires alternative can supplant that solution. That is what most people propose today.

The more comprehensive approach is to look at the full range of options to meet a constraint or need, and the full range of entities (customers, third party service providers, or the utility) that can implement those options. Planners should ask themselves questions like "Assume you are unable to build a feeder/transformer/etc. How will you meet this need?" The OEB could assist utilities by setting expectations for that type of more holistic planning.

Second, the OEB can promote evolution of the skillsets of system planners and utility executives. This can be done through the normal method of guidance and encouragement. The OEB can also be proactive in recognizing, establishing, certifying, or even funding training programs (no matter who offers them) that broaden the planning knowledge of utility personnel. Many professions have continuing education requirements. The OEB could implement similar requirements for system planning.

4. Is providing incentives to distributors to facilitate adoption of DER solutions (i.e., non-wires alternatives) appropriate? Under what circumstances?

SEC's starting point is that utilities should be expected to provide their services at the lowest possible cost, and should not be allowed to recover higher costs from customers because those capital options will generate higher utility profits.

For example, most utilities pay in their operating costs for many software applications they use on a day to day basis. They earn no margin on those costs, and nothing is in rate base. If a utility decided, instead, to build and own a proprietary word processing software package, adding it to rate base, neither the customers nor the regulator would accept that. The fact that rate base earns ROE, and operating costs do not, should not figure into the equation.

Comparing traditional solutions and non-wires alternatives should not be any different. If one alternative has a lower delivered cost to the customers than the other, the fact that the profit to the utility is different in the two cases should be irrelevant.

That having been said, it is Pollyanna thinking to assume that utilities will consistently reject tried and true traditional solutions with the knowledge that in doing so they are reducing their profits. For better or worse, utilities in Ontario are business corporations, in which maximization of profits is a fundamental goal.

SEC therefore believes that, in tandem with a hawkish approach to least cost planning, the OEB should test some modest incentives to see how they influence utility behavior. As long as the OEB signals to the sector that the primary rule is least cost planning, targeted incentives may support that goal in narrow cases.

5***. If incentives are appropriate, how should the OEB select/develop the form of incentive that should be available? a) Are there options the Incentive Subgroup did not identify that should be considered?***

While the OEB could design and implement its own pilots in this regard, in our view a better approach may be to invite utilities with significant DER activity to come forward with their own proposals, and consider them in an evidence/discovery/hearing environment. This has the initial benefit of the OEB seeing what incentives are sought by the utilities, and the subsequent benefit that there can be a thorough discussion with all stakeholders in the context of a specific set of DER solutions. Later followup will demonstrate whether whatever is ultimately approved was successful.

In our view, the list provided by the Incentive Subgroup is comprehensive.

However, SEC notes that the Subgroup Report included incentive options that should not be considered by the OEB.

Of particular concern to SEC is rate basing non-capital spending. We oppose this option for three main reasons:

- A significant barrier to DERs is the return on rate base approach to utility remuneration. Expanding return on rate base so that it includes operating costs appears to be an exacerbation of that problem, not a solution.

- Capitalization of DER costs will never be enough to match the capitalization of traditional solutions, since by definition the DER is the cheaper option. If the utility is not as well off with capitalized DERs as it is with the traditional solution, the disincentive remains. It is just reduced.

- Capitalization continues a problematic theme of basing profits on spending rather than on results. No other business in our society gets automatically rewarded for increased spending.

With that caveat, SEC believes that the OEB should be open to narrowly-targeted utility proposals, which can operate as pilot projects.

6. What should the OEB consider when setting expectations to ensure distributors appropriately consider DER adoption when planning and operating their systems (e.g., industry guidance, additional filing requirements for Distribution System Plans, new requirements for reporting and sharing information)?

SEC's responses to the previous questions cover a lot of this. We will add one thing.

It is important, in our view, for the OEB to communicate clearly and effectively that the sector is going to go through major changes in the coming (very) few years. In this period of change, the OEB should be looking at rate and other applications through the lens of change management. The OEB should identify the extent to which utilities are treating change as an opportunity to serve their customers better, rather than a problem to be resisted or "solved".

Utilities should therefore expect that their interactions with the OEB will be characterized by the regulator looking for proactive management that seeks every possible way of improving their product. It is perhaps trite to say that the expectation should be a focus on better customer outcomes, but in the context of an increasingly competitive and crowded sector, that opportunity-driven mindset should be what the utilities are seeking, and the OEB is expecting.

All of which is respectfully submitted.

Yours very truly,
Shepherd Rubenstein Professional Corporation

Jay Shepherd

cc: Brian McKay, SEC (by email)
Interested Parties (by email)