February 29, 2024

Nancy Marconi
Registrar
Ontario Energy Board
2300 Yonge Street, P.O. Box 2319
Toronto ON, M4P 1E4

Dear Ms. Marconi,

RE: EB-2023-0188 Evaluation of Policy on Utility Consolidations
Comments of Energy Probe on the OEB Staff Discussion Paper

In its letter of February 8, 2024, the OEB invited stakeholders registered to participate in the EB-2023-0188 consultation to provide written comments on all issues addressed in the OEB Staff Discussion Paper. The following are the comments of Energy Probe Research Foundation (Energy Probe).

Energy Probe agrees with most of the recommendations in the OEB Staff Discussion Paper, except as noted below.

Are Consolidations in the Public Interest?

The Staff Discussion Paper is based on the premise that consolidations are in the public interest. Energy Probe does not accept that premise. If public interest considerations include considerations of costs and rates, that premise has not been proven. Experience over that past decade has not demonstrated that consolidated utilities have lower unit costs or rates or provide better quality service.

One important aspect of public interest is control by locally elected officials. Energy Probe believes that the main reason that consolidation activities have slowed down is that municipalities believe that loss of local control of utilities is not in the interest of the public that elects municipal councils. Energy Probe believes that democratically elected municipal councils should have final say if consolidation of their local utility with another utility is in the public interest.

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No Harm Test

The imperative to consolidate utilities was based on the belief that there are economies of scale that can be achieved by consolidations of many smaller utilities into a few larger utilities. The expectation was that larger utilities would have lower per unit operating costs and ultimately lower rates. The experience so far indicates that that is not the case. There are dis-economies of scale with consolidated utilities, such as additional layers of management for larger utilities or higher transportation and travel costs if consolidated utilities are not contiguous.

It is not likely that two utilities will have identical rates prior to merger. After consolidation and rebasing it is likely that ratepayers of the utility with lower rates will have to subsidise ratepayers of the utility with higher rates to achieve rate harmonization. Ratepayers of the utility with higher rates pre-consolidation will benefit by having lower rates than they would have had if the consolidation had not occurred. When considering the no harm test, should benefits to one group of ratepayers offset the harm to another group of ratepayers? Energy Probe submits that they should not. No Harm Test should mean that no ratepayers are harmed.

The test is forward looking based on forecasts of future rates and service quality of the consolidated utility compared to the individual utilities prior to consolidation. Due to the 10-year deferred rebasing period it is likely that actual results will vary greatly from forecasts and promised synergies and productivity improvements will not be achieved. It is possible that the consolidated utility will have higher rates and poorer service quality than what was presented to the OEB in the consolidation application? What remedies are available to ratepayers? Can the consolidated utility be un-consolidated? Energy Probe believes that the option of separating consolidated utilities and restoring the pre-consolidation utilities should be available at the end of the deferred rebasing period as a remedy in cases where the promised savings and service quality consolidation were not achieved.

Deferred Rebasing Period

The deferred rebasing period of up to 10 years was put in place as an inducement to utilities to consolidate. This may have worked in the past, but it does not seem to be as effective now. Consolidation proposals have slowed down and there are still about 60 utilities regulated by the OEB. In many cases rates of pre-consolidation utilities continue during the deferred re-basing period. If the consolidated utilities did not re-base for several years prior to the consolidation, then the rates near the end of the 10-year rebasing period could be based on costs that are more than 10 years out of date.

As a basic principle, rates should be based on costs. Basing rates on 10-year-old costs escalated by a formula moves away from that principle. Eventual re-basing after a 10-year deferral is likely to result in a sharp increase in rates which may need to be mitigated over the next rebasing period. In those situations, rates would not be based on costs for many more years. Energy Probe believes that ratepayers should be charged for the cost of the service they receive so that they can make economically efficient decisions. If ratepayers are under-charged for the services, they receive they may use more of the service resulting in wasteful use of utility's assets and services.

Utilities requesting long deferred rebasing periods of up to 10 years, sometimes claim that they need this time to find synergies and productivity savings from consolidation. This claim is hard to believe. In industries not regulated by the OEB, managements of consolidated companies can find savings in a much shorter time, usually one year or less. If managements are not successful, they are replaced. Regulation is substitute for competition. A 10-year period where management looks for productivity savings from a consolidation would never be tolerated in the competitive market. Energy Probe submits that maximum length of the re-basing deferral period should be five years.

Incremental Capital Funding

The availability of incremental capital funding during the deferred rebasing period using the Incremental Capital Module (ICM) policy creates an incentive to overspend on capital. Utilities that spend more money than is available using existing rates as determined by the ICM Materiality Threshold, can apply to have the excess capital spending funded by ratepayers using ICM rate riders. The OEB's Price Cap rate setting policy provides and incentive to underspend on maintenance. Utilities that underspend on maintenance will appear to be more productive and can get a larger rate increase in a subsequent year. The long-term effect of these two policies is premature replacement of assets and higher rates. Energy Probe believes that the OEB should review its policies to remove incentives for overinvestment on capital and underspending on maintenance during the deferred rebasing period.

Respectfully submitted on behalf of Energy Probe.

Tom Ladanyi Digitally signed by Tom Ladanyi
Date: 2024.02.29 16:45:27 -05'00'

Tom Ladanyi
TL Energy Regulatory Consultants Inc.

cc. Patricia Adams (Energy Probe)
Georgette Vlahos (OEB Staff)