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January 7, 2025

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

Dear Ms. Marconi,

RE: EB-2024-0129 Advancing Performance-based Rate Regulation
Energy Probe Comments

The OEB held a stakeholder meeting on November 19, 2024, to discuss the actions the OEB can take to advance its performance-based approach to rate-setting. The OEB also invited stakeholders to provide written comments by December 13, 2024, which was later extended to January 8, 2025. Energy Probe Research Foundation (Energy Probe) attended the stakeholder meeting, and the following are its comments. The comments are organized as responses to specific questions raised by the OEB at the stakeholder meeting.

1.In the near term, the OEB plans to advance performance-based regulation by incorporating PIMs (performance incentive mechanisms) into the current framework. Informed by your review of the jurisdictional scan:

a. What do you see as the advantages and disadvantages (or opportunities and risks) of incorporating PIMs?

Energy Probe response
What matters most to customers is the cost of electricity. Yet, the jurisdictions included in the jurisdictional scan that have PIMs have higher electricity rates than Ontario. There are 50 states in the US. There are many with lower rates than Ontario. They should not have been excluded from the jurisdictional scan.

According to the CA's Jurisdictional Scan, Ontario has 59 electricity distributors. Of these only one is owned by outside investors while the other 58 are owned by municipalities. There are several municipally owned distributors in New York and California, two states that were in CA's

Jurisdictional Scan. In structure and ownership, they are very similar to the 58 municipally owned distributors in Ontario. CA did not provide any information on how they are regulated.

The advantages of PIMs are that they can focus on certain specific activities and outcomes. The disadvantages of PIMs that they can create excessive focus on certain activities and outcomes resulting in reduced attention to essential outcomes such as cost of electricity and reliability. PIMs are likely to complicate regulation of electricity distributors and end up increasing costs.

b. From your perspective, what are the most important considerations to keep in mind when developing PIMs? (e.g., measurability, simplicity, transparency).

Energy Probe response
It has not been proven that PIMs are needed. If the OEB decides to implement PIMs they should be simple, measurable, and transparent. They should also be appropriate to the size of the utility, its location and its customer base.

c. In your opinion, what outcomes do consumers value? (e.g., cost-effectiveness, reliability, customer service, enabling electrification, EVs, and/or DERs/NWSs).

Energy Probe response
Consumers are not a homogenous group. Most consumers value cost, reliability and customer service. A small and very vocal number of consumers value increased electrification, EV (electric vehicle) chargers, rooftop solar DERs (distributed energy resources) and NWSs (non wires solutions such as grid batteries. That small group is generally composed of more affluent and politically connected customers for whom cost is no object in their quest to achieve their largely political or social objectives. The OEB must not ignore the interests of the vast majority of electricity customers just to please a vocal minority.

d. To which outcomes or performance measures do you believe PIMs should be tied?

Energy Probe response
Energy Probe sees no need for PIMs. However, if the OEB decides to implement PIMs they should be tied to what matters most to the majority of customers: cost, reliability and customer service.

e. What PIM structure/design is likely to be most effective and most suited to Ontario, considering the existing rate-regulation framework? (e.g., $ value per participant/installation etc., awarded basis points if targets are met)

Energy Probe response
If the OEB decides to implement PIMs, they should impact the IRM productivity stretch factor.

f. Should PIMs be applied uniformly to all utilities, or should they be utility specific? Elaborate.

Energy Probe Response
If the OEB decides to implement PIMs, they should be uniformly applied to all utilities in the interest of fairness. However, PIM targets would be more difficult to achieve by some utilities than others, which would make the PIMs unfair. Designing utility specific PIMs would be difficult and may not achieve fairness anyway. Indeed, the problem of fairness is an important reason why the OEB should not implement PIMs.

g. What timeline would be appropriate for PIM implementation, and should there be a phased approach?

Energy Probe Response
Energy Probe sees no need for PIMs. However, if the OEB decides to implement PIMs, the appropriate timeline would be at rebasing of each utility. There would be no need for a phased approach.

h. How should baseline performance levels be established, and how frequently should targets be reviewed?

Energy Probe Response
If the OEB decides to implement PIMs, the baseline performance levels should be established in consultation with utilities and ratepayer representatives over at least a two year period. After that time, targets should be reviewed on an annual basis.

i. How should PIMs account for factors outside utility control (e.g., weather events)?

Energy Probe Response
Energy Probe sees no need for PIMs. However, if the OEB decides to implement PIMs, they should be implemented on a weather normalized basis specific to each distributor.

Questions – Fundamental Change

2.In the long term, the OEB is considering developing an approach to rate regulation that is no longer premised on rate base rate-of-return.

a. Is this fundamental change required? Why or why not?

Energy Probe Response

Energy Probe believes that this fundamental change is not required. OEB current approach to rate regulation is working well and can be improved by small changes that would reduce the bias that currently exists in favour of spending on capital instead of on maintenance.

Each year, the OEB benchmarks electricity distributors' total cost performance. The rankings from the benchmarking results for the current year's electricity distributors are used to assign stretch factors. The stretch factor forms part of the annual Incentive Rate Mechanism (IRM) process and is used to determine how a distributor's rates will be adjusted.

As the OEB explained[1] in its letter of August 6, 2024, "incentive rate setting rewards distributors based on their total cost performance; i.e., the better the cost performance, the better the reward. Based on ranking, each distributor is assigned to one of five cohorts, with the best cost performers in Cohort I and the lower cost performers in Cohort V. The distributors in Cohort I as the best performers are rewarded with no rate reduction adjustment. The distributors in the lower cohorts receive reduction adjustments ranging from 0.15%in Cohort II to 0.60% in Cohort V. The stretch factors are designed to incent distributors to perform better, and as such, promote, recognize and reward distributors for cost efficiency improvements, which in turn lead to lower distribution costs and rates." Stretch factor assignments are based on updated results of the November 2013 Report [2] to the OEB by the Pacific Economics Group ("the 2013 PEG Report").

The unintended consequence of OEB benchmarking is that it creates a bias in favour of capital instead of maintenance spending. Distributors can improve their performance by reducing spending on maintenance, or by outsourcing work to affiliates that do not follow MIFRS (Modified International Financial Reporting Standards) that the OEB requires distributors to follow. MIFRS do not allow capitalization of costs that can be capitalized under GAAP (Generally Accepted Accounting Principles). This allows affiliates of distributors to capitalize costs that the distributors would have had to treat as maintenance costs. By doing this, distributors can appear to be more productive than they are and be in a Cohort where they do not deserve to be.

Energy Probe proposes that the OEB change its benchmarking method to remove the bias against spending on maintenance in favour of capital that is in the 2013 PEG Report. This can be done by changing the weighing factor for maintenance expenditures in the benchmarking formula in the 2013 PEG Report. This may require a review of and revision of the 2013 PEG Report. The OEB should also require that affiliates of distributors which perform services for distributors follow MIFRS.

[1] Incentive Rate Setting: 2023 Benchmarking Update for Determination of 2024 Stretch Factor Rankings - Board File No.: EB-2010-0379, August 6, 2024

[2] Productivity and Benchmarking Research in Support of Incentive Rate Setting in Ontario - Final Report to the Ontario Energy Board, Pacific Economics Group, November 2013

b. How would this fundamental long-term change impact stakeholders in the sector, both throughout its development and upon implementation?

Energy Probe Response
Energy Probe believes that its proposals would result in distributors increasing maintenance spending which would improve reliability of the distribution system. In the short term rates may increase but would be lower in the long run. Energy Probe believes that electricity ratepayers would be better off.

Since Energy Probe's proposals would change benchmarking, some distributors would end up in a different Cohort than where they would have otherwise been. Some distributors would be better off, and some would be worse off.

c. What transition measures could be put in place to provide stability during a period of change?

Energy Probe Response
Energy Probe believes that its proposals would not require any transition measures.

d. Are there quick wins that the OEB can advance in the short term?

Energy Probe Response
Energy Probe believes that its proposals can be implemented within one year or at rebasing of each distributor. That would make the proposals a quick win.

Respectfully submitted on behalf of Energy Probe.

Tom Ladanyi
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Tom Ladanyi
TL Energy Regulatory Consultants Inc.

cc. Patricia Adams (Energy Probe)