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Registrar
Ontario Energy Board
2300 Yonge Street, 27th floor
Toronto, ON M4P 1E4

Re: Advancing Performance-based Rate Regulation – Performance Incentive Mechanisms (PIMs) (EB-2024-0129)

Toronto Hydro-Electric System Limited ("Toronto Hydro") is the local electricity distribution company for the City of Toronto. It serves over 790,000 customers and delivers approximately 18% of the electricity used in Ontario.

On May 14, 2025, the Ontario Energy Board ("OEB") released a Discussion Paper presenting draft performance incentive mechanisms ("PIMs") for electricity distributors as part of its consultation to advance its performance-based approach to rate regulation. The Discussion Paper proposes four PIMs for stakeholder feedback, with the goal of strengthening the link between what electricity distributors earn and the achievement of outcomes consumers value. On June 3, 2025, the OEB held a stakeholder consultation to present its findings of the Discussion Paper and obtain stakeholder feedback on the following proposed PIMs:

1) System Capacity / Electrification (Load Factor)
2) Reliability (System Average Interruption Duration Index)
3) Reliability (System Average Interruption Frequency Index)
4) Efficient Connections (Average time of requested customer DER connection)

Toronto Hydro supports the OEB's ongoing commitment to modernizing and advancing performance-based regulation and welcomes the opportunity to provide the responses and observations below. Toronto Hydro is an active member of the Electricity Distributors Association ("EDA") and supports and is broadly aligned with its respective submission on these issues.

Ontario's electricity system is entering a period of unprecedented change. Demand is projected to grow by roughly 75 percent over the next 25 years, propelled by record housing construction, industrial

expansion and the electrification of heat and transport[1]. In response, the Government of Ontario has released *Energy for Generations*—its first integrated energy plan[2]—and introduced Bill 40, *Protect Ontario by Securing Affordable Energy for Generations Act, 2025*[3]. Both instruments commit the Province to four key objectives: affordability, security, reliability and clean energy.

In this context, Toronto Hydro believes the OEB's exploration of the development PIMs is not merely timely, but essential. As noted in Toronto Hydro's recent letter to the OEB[4], compared to other ongoing OEB consultations such as Total Cost Benchmarking ("TCB"), a properly designed PIM framework can sharpen accountability, reward excellence, and make the value of utility performance more transparent to customers, strengthening public confidence in the process.

From Total Cost Benchmarking to a Modern PIM Framework

While TCB has helped the Board gauge historical cost performance, its complexity and historical construct limit its practicality in today's era of rapid electrification and large-scale grid investment. TCB does not clearly connect the dollars customers pay for the tangible outcomes they receive. In contrast, PIMs can make that linkage explicit—tying incremental earnings to discrete public-interest objectives. A comparable reward-only orientation has been adopted in jurisdictions such as the state of New York, where reward-only PIMs have been used to focus utility effort without undermining basic cost-recovery[5]. By shifting regulatory emphasis from historical spending patterns to measurable customer and policy outcomes, PIMs can better guide distributors as they navigate rapid load growth, capacity expansion, and DER integration. Toronto Hydro urges the OEB to prioritize the development of a robust, reward-focused PIM framework as an evolution and replacement for TCB, which it views as a legacy tool whose relevance is rapidly diminishing in today's investment-intensive, policy-driven environment.

Approach to PIM Development

Toronto Hydro supports a transparent, evidence-based PIM framework that rewards superior customer outcomes. However, successful implementation in Ontario requires three foundational design choices:

[1] Independent Electricity System Operator, 2025 Annual Planning Outlook, page 2.
[2] Ministry of Energy and Mines, "Energy for Generations", June 12, 2025.
[3] Legislative Assembly of Ontario, "Bill 40, Protect Ontario by Securing Affordable Energy for Generations Act, 2025", June 3, 2025.
[4] Toronto Hydro, May 26, 2025 Letter to the OEB with regard to Total Cost Benchmarking
[5] Christensen Associates, "Jurisdictional review of Utility Remuneration Models for the Ontario Energy Board", September 2024, page 29.

a customer centric, locally validated, custom approach; voluntary, asymmetrical-positive PIMs; and a framework that aligns with Government priorities.

Customer Centric, Locally Validated, Custom Approach

Ontario's approximately 60 local distribution companies ("LDCs") serve communities that differ profoundly in customer density, asset age, climate exposure, and socio-economic profile. A condominium owner in Toronto proper, an industrial factory in Northern Ontario, and a rural greenhouse operator in Southern Ontario value different aspects of service and at different times. Toronto Hydro's own engagement processes demonstrate that customers want tailored solutions—whether that is accelerated EV-charger connections, superior outage communications, or targeted power-quality programs. A single, mandatory set of PIMs would therefore misalign incentives for many utilities in relation to what their customers value. For example, reliability may be relatively more important to customers in a certain region versus others; it is flawed to assume priorities are uniform across the entire province. A rural customer may value reliability different than a customer in an urban setting, as both customer priorities and existing service levels vary widely between rural and urban systems. Applying consistent reliability incentives across Ontario would overlook those important differences. Allowing utilities to tailor both its choice of metrics and its targets keeps incentives aligned with what local customers value most and sparks innovation where it is truly needed.

A locally validated framework is also more transparent to the public. Customers can see a direct line from the survey responses they provided to the incentive that drives utility actions, and as a result see a set of goals that they recognize as relevant to their own experience. In Toronto Hydro's experience, that transparency strengthens trust far more than a pre-determined, abstract index like TCB.

The OEB's Discussion Paper proposes a package of capacity, reliability, and DER-integration metrics. Generic approaches may simplify benchmarking, implementation, and administration, but it risks either ignoring local priorities or forcing utilities into costly workarounds to avoid penalties that do not reflect customer preferences. To address this, Toronto Hydro is a proponent of adopting a voluntary opt-in approach to PIMs. Each distributor should be able to propose a voluntary portfolio of PIMs calibrated to its engagement evidence and filed as part of its next rebasing or Custom Incentive Rate ("CIR") application. The OEB already expects such engagement in respective rate filings; PIMs should build on, not replace, that discipline.

Upside-only rewards, tied to locally validated metrics, will deliver clearer value to customers than schemes that impose penalties divorced from local priorities. The OEB's Discussion Paper highlights various stakeholder feedback that emphasizes the importance of tailoring metrics to utility circumstances[6], and a voluntary approach simply extends that logic. Allowing each LDC to propose a bespoke set of targets tied to its customer priorities is the fairest and most efficient path forward.

Fair Return Standard and Financial Integrity: Asymmetrical-Positive PIMs

Ontario's cost-of-capital formula yields an allowed return on equity ("ROE") that the OEB has judged to satisfy the Fair Return Standard ("FRS")[7], providing what has been deemed an appropriate level of return for the risk being undertaken by utilities in fulfilling their license conditions. Toronto Hydro notes that any penalties layered on top of that approved revenue will, by definition, lower earned returns below the FRS, increase financing costs, and ultimately raise customer bills. The OEB's annual cost of capital letters confirm that each annual ROE update must continue to meet the FRS[8]; inserting additional downside risk without an offsetting ROE adjustment would violate that principle. Simply put, there is no justification for applying either an asymmetrical-negative or symmetrical penalty framework for utility risks that are already factored into the establishment of the ROE. Reward-only incentives avoid this problem; it preserves the base ROE and motivates superior performance through upside potential. Moreover, as rating agencies typically treat penalty exposure as an additional business-risk factor, limiting exposure only to upside rewards ensures that this framework does not inadvertently erode utility credit ratings or increase borrowing costs.

Some intervenor groups may argue for symmetrical "carrot-and-stick" mechanisms on the grounds of fairness. Toronto Hydro submits that the "stick" already exists in the form of mandatory service-quality requirements, OEB audit powers, etc. Imposing additional financial penalties for obligations utilities must already satisfy would simply punish them twice for the same baseline requirement. In contrast, an upside-only reward is logically sound as it incentivizes utilities to go beyond the established standard rather than duplicating enforcement tools that are already effective. Layering a second set of financial penalties on top of those tools is neither necessary nor prudent.

[6] OEB Staff Discussion Paper – Performance Incentive Mechanisms, page 15.
[7] OEB March 27, 2025, Decision and Order of Cost of Capital and Other Matters Generic Proceeding
[8] OEB Letter re: 2025 Cost of Capital Parameters, page 2, "The OEB Report stated that each time a formulaic approach is used to calculate an allowed ROE, it must generate a number that meets the Fair Return Standard, as determined by the OEB using its experience and informed judgment."

The province is entering a historic investment cycle and utilities are being asked to expand capacity rapidly. Therefore, Toronto Hydro urges the OEB to adopt an asymmetrical-positive structure—rewards for exceeding targets, but no penalties for shortfalls—as the only approach consistent with maintaining the financial integrity required to fund Ontario's growth agenda[9], which is further explored below.

Interplay with Provincial Government Priorities

The Government of Ontario has very recently issued an unprecedented wave of policy direction. *Energy for Generations* – Ontario's first Integrated Energy Plan and Bill 40, *Protect Ontario by Securing Affordable Energy for Generations Act, 2025*, backed by ministerial directives, instruct distribution utilities to manage multiple priorities including housing expansion, load growth and capacity, electrification, resiliency and reliability, and the facilitation of distributed energy resources, among others.

Against this backdrop, OEB's June 3rd stakeholder consultation highlights four mandatory PIMs on load factor efficiency, DER-connection timeliness, and penalty-only reliability (SAIDI/SAIFI) metrics. However, some the proposed PIMs seem to pull in different directions, contradicting both with one another and with the broader priorities set by the provincial Government. For example, a System Capacity / Electrification – Load Factor PIM that rewards high utilization could discourage distributors from building the very headroom that Bill 40 and the IEP demand to build new feeders, accommodate housing expansions, and connect large loads such as battery factories and hydrogen hubs. Aligning PIM metrics explicitly with Government priorities such as the ones listed in the various directives and rejecting metrics that contradict them would prevent such inconsistencies. Toronto Hydro recommends the OEB to begin by explicitly mapping Government, regulator, stakeholder and customer objectives, and give utilities the flexibility to propose a set of PIMs that align with the top tier of that hierarchy.

Finally, the interaction of PIMs with existing regulatory tools (i.e. Incremental Capital Modules, Distribution System Plans) must be mapped carefully. Without such mapping, distributors could face simultaneous funding reductions through negative PIM payouts while being obliged to invest heavily under government mandates, creating a "snowplow" of deferred projects caused by constrained funding and escalating long-term costs. More specifically, if incentives are neither grounded in utility specific plans nor informed by local experience, the real-world effects are impossible to predict with

[9] Bill 40's preamble commits to "building an affordable, secure, reliable and clean energy system to power the strongest economy in the G7".

confidence. To avoid PIM penalties, projects meant to deliver government-mandated outcomes could be deferred or downsized. Unless the OEB explicitly maps each incentive to provincial goals and models those trade-offs in advance, the Province could find that the very initiatives it deemed urgent end up chronically underfunded if a penalty-based framework takes effect.

Implementation Considerations

To ensure that any new PIM framework is both rigorous and practical, several foundational implementation steps are essential. First, clear baselines should be established. Toronto Hydro broadly supports the OEB's recommendation to establish targets based on the utility's historical performance. Moreover, for every metric, baseline performance should be anchored in 5-years of historical data, if available, while also taking into account expected future business conditions (e.g., rapid load growth or major asset-renewal programs). This approach provides a statistically sound starting point and prevents short-term anomalies from distorting targets. Targets should be reviewed every 5 years in alignment with rebasing applications and distribution system plans (as applicable).

Second, target reviews should align with the regulatory cycle. Performance targets should be reviewed every five years, coinciding with rebasing applications and the filing of Distribution System Plans. Aligning PIM recalibration with these milestones will streamline stakeholder review and ensure that incentives evolve in step with system needs and customer expectations. With respect to determining target values, Toronto Hydro cautions the OEB and its recommendation to use existing OEB working groups. Repurposing existing working groups would be ill-suited as they were initially formed for completely different purposes and might not be well-equipped for this task. While Toronto Hydro would gladly participate in a new OEB-led working group, it offers the following perspective for consideration albeit without an explicit solution. Experience shows that multi-utility forums often gravitate to "middle of the road" incentive levels that do not particularly fit any one distributor well, over incentivizing some while under incentivizing others, and diluting the very signal PIMs are meant to send.

Lastly, if the OEB intends to proceed with the timelines proposed in the Staff Discussion Paper, Toronto Hydro suggests a feasible implementation timeframe be given to enable proper consultation and adoption, specifically on PIMs in relation to load factor and DER connection timeliness. Utilities will need sufficient lead time, typically 18-24 months, to conduct stakeholder consultations, integrate new data-tracking systems, and embed PIM metrics into business planning. A phased or "shadow-year"

approach offers the safest on-ramp: for the first one to two years, utilities would track proposed PIM metrics and publicly report results without financial consequences. This pilot period allows distributors to test data integrity, uncover unforeseen implementation issues, and refine methodologies before full-scale deployment. By combining robust historical baselines, a regular five-year review cadence, and a phased rollout, Ontario can introduce PIMs that are ambitious yet manageable, safeguarding both customer interests and utility operational stability.

Toronto Hydro appreciates the opportunity to continue to work with the OEB and stakeholders to advance performance-based approach regulation, specifically around the development of Performance Incentive Mechanisms to enable outcomes that consumers value such as cost effectiveness, reliability, and customer service, while ensuring alignment with Government priorities.

Respectfully,

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