



**BY EMAIL and RESS**

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Our File: EB20250108

**Attn: Ritchie Murray, Acting Registrar**

Dear Mr. Murray:

**Re: EB-2025-0108 – Spending Pattern Analysis Factor – SEC Comments**

We are counsel to the School Energy Coalition (“SEC”). These are SEC’s comments on the OEB Staff Report on Spending Patterns and Capitalization Policy (“Report”) prepared by Pacific Economic Group (“PEG”).

SEC commends the OEB for undertaking this initiative. Empirical analysis is critical to understanding electricity distributor behavior, as it impacts the success or failure of the OEB’s core function of rate-setting and to protect the interest of consumers with respect to price.

**Comments on Spending Patterns**

Generally speaking, SEC agrees with the findings in the Report regarding electricity distributor spending patterns, which are consistent with our observations over the years from our participation in most rate applications before the OEB. For distributors on a Price Cap rate-setting framework, SEC has often observed, in the lead up to a rebasing application, significant increases in both capital and OM&A expenditures, whereas in the years after a rebasing application test year, there are much smaller year-over-year increases, and sometimes decreases in spending. For distributors on Custom IR, we agree with PEG that these spending patterns are less prominent<sup>1</sup>, but that is because the rate-setting framework that is significantly more generous in terms of remuneration, to the detriment of incentives for cost control. Put another way, the fact that distributors on Custom IR do not exhibit these patterns, is symptomatic of much larger problems compared to Price Cap IR.

Moreover, from SEC’s perspective, the cost control aspect of capital is the greater problem, although the reasons for the increase in certain situations are legitimate and so it is difficult to come to any significant conclusions. The OEB should investigate the matter further, with a specific focus on understanding what types of capital expenditures are increasing faster late in a rate term. Is it the system access category, where a distributor has significantly less discretion, or is it other categories

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<sup>1</sup> Report, p.19

where they have much more? At the same time, the inherent rate-setting structure which provides a return on equity (“ROE”) on capital additions, creates a natural incentive to overspend.

As some stakeholders noted<sup>2</sup>, and SEC agrees, the OEB does not usually disallow capital costs from rate base that have already been incurred, absent a true finding of imprudence on an individual project basis as a result of mismanagement or true lack of project need. Distributors know this and will overspend in excess of their previous set plan, recognizing that the effective ROE on those expenditures over its lifetime, even with the foregone revenue during the remainder of the IRM term, is often immaterial and will still result in a very healthy return.

In the Report, PEG has provided a list of potential remedies to address the concerns the evidence shows regarding problems with distributor spending patterns.<sup>3</sup> They all deserve consideration as part of the OEB's Next Generation Rate Framework consultation<sup>4</sup>, however, piecemeal solutions like an Efficiency Carryover Mechanism (“ECM”)<sup>5</sup> are often very complicated to implement at the specific distributor level, may result in more harm than good to ratepayers, and offer a new avenue for gaming. For example, we note that as part of the Alberta Utilities Commission's most recent PBR framework, it eliminated the ECM that had been part of the previous PBR framework, finding that it did not achieve its intended purposes of addressing the weakening cost control incentive towards the end of a plan.<sup>6</sup>

These are issues that should be part of the broader discussion in the OEB's consultation on the Next Generation Rate Framework, which must include not just the proposed remedies set out in the Report, but broader consideration of the lack of cost control measures throughout the existing rate-setting options.

### **Comments on Capitalization Policy**

The Report discusses electricity distributors changing their capitalization policies during their rate term.<sup>7</sup> In SEC's experience, such changes are in fact rare. It is arguable whether a change is even permitted currently, but even if it is, the changes are reviewed at rebasing, and the ratemaking implications can be reversed by increasing or decreasing opening rate base.

What is more likely to happen, and harder for the OEB and intervenors to detect, is a change in the interpretation of existing policy. The OEB may consider requiring, as part of cost of service filing requirements, that utilities outline any changes to how they interpret their capitalization policies and quantify the resulting impact.

Yours very truly,  
**Shepherd Rubenstein P.C.**

Mark Rubenstein

cc: Brian McKay, SEC (by email)

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<sup>2</sup> Report, p.78-79

<sup>3</sup> Report, p.94-104

<sup>4</sup> EB-2026-0002

<sup>5</sup> Report, p.100

<sup>6</sup> Alberta Utilities Commission, Decision 27388-D01-2023 (October 4, 2023), p.97

<sup>7</sup> Report, p.50