AMPCO

December 15, 2008

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319, 27th Floor
2300 Yonge Street
Toronto, Ontario M4P 1E4

Dear Ms. Walli:

Re: Further Consultation on Stretch Factor Rankings for 3rd Generation Incentive Regulation for Electricity Distributors
Board File No. EB-2007-0673

Attached please find AMPCO's comments on the Board staff paper.

Sincerely yours,

Adam White

Copies to: Participants

Association of Major Power Consumers in Ontario
www.ampco.org

372 Bay Street, Suite 1702
Toronto, Ontario M5H 2W9

P. 416-260-0280
F. 416-260-0442

Comments

Re: Further Consultation on Stretch Factor Rankings for 3rd Generation Incentive Regulation for Electricity Distributors OEB File: EB-2007-0673

This update from PEG is helpful primarily for providing some perspective on the robustness of the methodology that PEG has employed.

AMPCO believes that the number of criterion used to categorize LDCs is unnecessary. Some criteria, such as latitude, have obvious effects on LDC efficiency. However, other factors such as customer count and proportion of underground plant are ultimately within the control of management and owners, and should not in principle lead to allowances with respect to peer selection.

Cohort selection criteria in general can be seen as an explanation for performance (good or bad), when adapting to external factors is one of the expectations of good managers. As an example from industry, no one suggests that Japanese vehicles should be more expensive because Japan lacks the natural energy and material resource advantages of its American competitors.

Notwithstanding the above, the PEG results appear to hold up well in the sensitivity tests. AMPCO recommends using the ranking that includes the 26% LV allocation, divided by 2.35 for embedded distributors.

A review of the OM&A cost indices for the LDCs does seem to suggest that both improvement and deterioration can occur in relatively short time frames, suggesting that in most cases management should not be overwhelmed by the modest stretch factors in this generation of IRM.

Ultimately, the purpose of IRM from a customer perspective is to provide an incentive to good management and cost control, whatever business the regulated entity is in. Looking only at the Unit OM&A cost indices, this does not seem to be happening so far. Of the 80+ LDCs reviewed, more than half (45) had their highest OM&A index results in 2007, while only 6 showed their lowest results in 2007. It may be that the PEG methodology does not properly account for inflation, or some other factor is skewing the calculations to produce an incorrect apparent trend over time. However, if the PEG results are in fact valid for year over year comparisons, then this trend indication should be cause for concern.

As a suggestion, the PEG results should be updated annually to support an analysis of how well IRM is working.

Finally, this effort should be placed in the context of the economic circumstances now unfolding for the customers of Ontario's LDCs. For at least the next year or so and probably for much longer, businesses that wish to survive in competitive environments will face severe pressure to cut cost and improve productivity. In turn, businesses will place equally severe pressure on their suppliers to control costs. LDCs should not be sheltered from this need.

If good regulation is intended to provide a meaningful substitute for competition, then the Board should consider much larger stretch factors for LDCs than the very modest targets contained in this proposal.

Prepared for AMPCO by:

C. W. (Wayne) Clark, P. Eng
San Zoe Consulting, Inc.
December 12, 2008