

## **COMMENTS OF THE CONSUMERS COUNCIL OF CANADA**

### **Re: Board Staff Research Paper on the Affiliate Relationships Code for Electric Distributors and Transmitters – EB-2007-0662**

#### **Introduction:**

On June 15, 2007, the Ontario Energy Board (Board) initiated a consultation process regarding its Affiliate Relationships Code for Electricity Distributors and Transmitters (Electric ARC). Specifically, the Board is seeking comments on the Board Staff Research Paper (Staff Paper) dated June 15, 2007, which provides background on the development of the Electricity and Natural Gas ARCs in Ontario, summarizes the current status of the Ontario electricity distributor affiliate relationships and identifies concerns regarding the Electricity ARC that have been recently raised by stakeholders.

These are the comments of the Consumers Council of Canada on the Staff Paper. The Council will first provide some general observations regarding the Electric ARC and then address some of the specific questions set out in the Staff Paper.

#### **General Comments:**

When regulated utilities establish affiliates it is critical that regulators set up rules and standards to ensure the interests of the regulated utility ratepayers are protected. In Ontario, where the Board regulates over 80 distributors and transmitters, most of which have affiliates, the need for an Electric ARC is clear. The Council agrees that the primary objectives of an ARC are to:

1. Prevent the cross-subsidization of affiliates by the regulated components of the business;
2. Protect and regulate the sharing of confidential customer information; and

3. Prevent affiliates from gaining improper advantages through affiliation with the regulated entity.

From the Council's perspective these objectives should be paramount to any other objectives adopted by the Board. In determining the elements of the ARC the following other issues should be considered:

1. The Natural Gas ARC and the Electric ARC should be consistent to the extent possible.
2. Monitoring and reporting on affiliate relationship issues is important and essential but the costs of such reporting should not outweigh the benefits;
3. There should be an established process that allows LDCs to apply for exemptions to be considered by the Board on a case by case basis.

#### **The Role of Utility Efficiency in the Electricity ARC:**

Board Staff is seeking input on whether it would be useful to include in the purpose section of the ARC "efficiency" as an explicit objective. Specifically, they are seeking views as to the degree to which promotion of the goal of efficient operations should be considered when developing and applying the Electric ARC provisions and restrictions.

The Council accepts that efficiency in utility operations is important and should always be consideration before the Board in setting rates. The 2005 *OEB Act* identifies economic efficiency as an objective for the Board to consider in its regulation of the electricity sector. The Council is not opposed to including a reference to efficiency in the Electric ARC, as long as it is clear that the primary objectives of minimizing cross-subsidization, regulating the sharing of customer information and preventing unfair treatment of affiliates remain paramount.

### **The Role of Competition in the Electricity ARC:**

The Council agrees that the Board should continue to have a role in protecting consumers from the utility abusing its monopoly power or its affiliates engaging in anti-competitive behaviour as a result of its relationship with the monopoly utility. Accordingly, the Council would support changing the ARC to reflect this role. The Council does not believe the Board should have a direct role in promoting the development of a competitive market.

Board Staff is seeking input at to whether there should be a distinction between the categories of markets that the utilities should be involved in and the role of the Board with respect to those markets. The oversight of the Board regarding energy services should be to limit anti-competitive behaviour and to ensure that any cross-subsidization is minimized to the extent possible. With respect to non-energy related goods and services, like telecommunications, the Council does not believe that the Board has a role in dealing with competition related issues in these markets. In that context the Board should only be concerned with the cross-subsidization issues and the use of customer information.

### **Treatment of Confidential Customer Information:**

Board Staff is seeking input on whether the current definition of confidential customer information should be narrowed. The Electric ARC currently requires information confidentiality in standard service agreements between distributors and their affiliates. The Council does not see any rationale for changing the current rules. As noted by Board Staff the current framework provides maximum protection to utility customers. From the Council's perspective relaxing the rules in any way that may jeopardize that protection would not be appropriate.

**Employee Sharing:**

The Council is not aware of the challenges faced by the Electric LDCs regarding the ARC provisions around the sharing of employees. In addition, it is not clear to what extent there is employee sharing between the LDCs and their affiliates. From the Council's perspective unless the LDCs can make a strong case to allow for more relaxed and less specific sharing rules the Board should adopt the provisions set out in the Natural Gas ARC related to this issue. It provides greater clarity to the LDCs and has proven effective in the natural gas sector.

It may be appropriate for the Board to consider this issue in more detail once the various submissions by the LDCs are received. The Board needs to balance the need to minimize cross-subsidization and protect the customers against the practical considerations that arise when employees are shared. We accept that efficiencies can be achieved when employees are shared reducing the overall revenue requirement of the LDC. If this can be done while also ensuring the interests of the utility customers are protected it should be permitted.

**Independent Directors:**

As noted by Board Staff the primary purpose of the provision in the Electric ARC requiring a minimum number of independent directors for a utility is to ensure that utility-related decisions are taken independently if affiliate interests and in the interests of ratepayers. The current rule is that at least one-third of an LDC's Board of Directors should be independent from any affiliate.

The Council is of the view that increasing the number of independent directors to at least 50% would be in the best interest interests of the LDC's customers. The argument against this requirement is that it would increase the cost of service. The increased cost relative to the added protection for ratepayers would not be significant.

Without such a requirement there is no guarantee that the interests of the affiliate would not take priority over the interests of the utility.

### **Transfer Pricing Rules:**

The transfer pricing rules have been put in place to ensure that the LDC does not pay more than it should to its affiliate for products and services and does not provide a product or service to its affiliate at a subsidized cost. The Natural Gas ARC has detailed provisions set out regarding transfer pricing that have recently been reviewed and clarified. The Council supports an approach that would have the Electric ARC mirror the Natural Gas ARC with respect to this set of issues. As noted by Board Staff extending the Natural Gas ARC rules to the electricity sector would expand ratepayer protection and restore consistency between natural gas and electricity sectors.

### **Outsourcing Utility Activities to an Affiliate:**

With respect to the issue of outsourcing the Council supports consistency between the gas and electricity sectors. In particular, there should be an explicit requirement for a business case before the costs arising from an outsourcing arrangement are presented to the Board for approval. In addition, the length of an affiliate contract should be limited to a five-year period. The Council also supports the addition of a provision that requires market tendering where a competitive market for the services exists. These provisions will clearly add protection for ratepayers and ensure that cross-subsidy of the affiliate by the LDCs is minimized to the extent possible.

### **Application of the Electricity ARC to Small Distributors:**

The ratepayers of small LDCs should be afforded the same regulatory protection as larger LDCs. There is no obvious reason why smaller LDCs should not be required to comply with the Electric ARC. As noted above, the Council supports the existence of an exemption process which would allow smaller LDCs to make a case before the Board for

exemptions. In addition, we support the view of Board Staff that more information should be made available on the criteria and process for an exemption request. The process should be sufficient to protect the interests of ratepayers, but not too costly and onerous for the LDCs to comply.

All of which is respectfully submitted.

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