Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street
26th Floor, Box 2319
Toronto, ON M4P 1E4

February 13, 2007

Dear Ms. Walli

Re: Staff Discussion Paper - Proposed Regulatory Framework for Conservation and Demand Management by Ontario Electricity Distributors in 2007 and Beyond (EB-2006-0266)

PowerStream Inc., Hydro Ottawa Limited, Enersource Hydro Mississauga Inc, Horizon Utilities Corporation, Veridian Connections Inc. and Toronto Hydro-Electric System Limited (collectively the "CLD") welcome the opportunity to comment on the Board Staff's Discussion Paper regarding the Proposed Regulatory Framework for Conservation and Demand Management by Ontario Electricity Distributors in 2007 and beyond. The paper provides distributors with a good understanding of the regulatory mechanisms designed to protect LDCs against distribution load reductions associated with CDM programs and other issues relevant to distributors.

In determining the next steps in the Board's consultation process, the CLD offers the following comments for Board staff's consideration:

Issue

The framework that staff is proposing for the dual funding model implicitly encourages LDCs to seek funding from the OPA, and to rely on funding through distribution rates where OPA funding is not available or where funding through distribution rates is more appropriate.

Comments

1. The CLD agrees with this proposal and would encourage the OPA and/or the Board to establish *a priori* criteria of what should be considered appropriate for OPA funding. Effective definition of responsibilities in this area will assist in CDM planning and minimize situations in which responsibility for program approval is unclear.
2. As the CLD understands the recommendation of the Board, any CDM program that is funded through electricity distribution rates will be subject to risks associated with demonstrating the prudence of underlying costs, which is consistent with the present methodology applied by the Board for determining just and reasonable rates. LDCs may view such risks to be greater than those underlying the delivery of OPA funded programs. In this circumstance, LDCs may shift their accountability related to CDM costs from rate customers and rely entirely on the OPA as a source for financing CDM programs.

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3. The CLD also supports the Board recommendation that CDM activities in which electricity distributors engage, regardless of the source of funding, must be consistent with the findings of the OPA's Integrated Power Supply Plan ("IPSP"). Under this construction the OPA's accountability for the overall plan is kept intact and the desired types and levels of CDM performance has context, with respect to the combined price for generation, distribution and transmission.

4. Some programs being proposed by the OPA will be for capital assets to support CDM (eg. Peak Saver). The OPA has indicated that the initial contracts will be for a 1-year period. It is unclear whether such contract would cover only funding for the required capital expenditures or whether such would include the provision of ongoing operating costs and a shareholder incentive. The Board recommendation on this matter does not clarify the ongoing operating costs and related shareholder incentives if the OPA contracts do not provide for such.

Issue

Board staff recommends that the Board continue to make the current form of LRAM available to LDCs in the near-term and, thereafter, consider longer-term alternative mechanisms to address lost revenue in the process towards the development of 3rd Generation IRM or the review of options for the fundamental redesign of electricity distribution rates.

Comments

5. To meet the Government's targets shareholder-funded (3rd tranche) programs, distribution rate funded programs, OPA-funded programs and 3rd party programs are estimated to have an imminent and marked effect on LDC distribution revenues. Therefore the CLD supports Staff's recommendation in Section 4.1.2 (Revenue Protection) that "the Board continue to make the current form of LRAM available to LDCs to address revenue erosion resulting from LDC CDM activities, regardless of whether the programs are funded by the OPA or through distribution rates."
6. However, the LRAM approach may not be appropriate or practical for all LDCs, and particularly those that may not have their distribution rates rebased until 2009 or 2010. Furthermore, the LRAM approach ignores the effect that 3rd party programs will have on an LDC's revenue. The CLD therefore suggests that the Board consider the merit of adopting the Hydro One proposal for a "Z-type" factor within the formula for 2nd Generation IRM. Details are provided in the EDA submission.

Issue

Board staff recommends that the Board should not provide shareholder incentive mechanism for CDM activities funded through the OPA – but that the OPA consider the inclusion of an incentive mechanism in its design of LDC CDM resource contracts;

Comments

7. The appropriate shareholder incentive mechanism should be developed in concert with the mechanism contained in the OPA contracts to ensure that incentives of CDM programs funded through distribution rates do not create a bias towards favouring programs funded through the OPA (or vice versa). So long as OPA contracts provide appropriate incentives for CDM, the CLD

notionally supports the direction being proposed by Board staff. However, in the absence of information about what form of incentive will be included in OPA contracts, it is difficult to assess their effectiveness or complement with SSM-type incentives.

8. The CLD strongly agrees with London Economics Inc. ("LEI")'s report that it is unreasonable to expect LDCs to pursue programs which provided no financial return for their shareholders; and that it is important to emphasize that any incentive needs to be in addition to the normal allowed return, otherwise it does not serve as an incentive at all.

Issue

Revenues earned from OPA CDM contracts be kept separate from the LDC's distribution revenue requirement;

Comments

9. The CLD strongly supports that the revenue earned from OPA CDM contracts is not considered revenue offset.

Issue

Any net revenues generated by a shareholder incentive for distribution rate-funded CDM would be separate from (i.e. over and above) the LDC's distribution revenue requirement.

Comments

10. The CLD would support a proposal where any net revenues generated by a shareholder incentive for distribution rate-funded CDM would be separate from (i.e. over and above) the LDC's distribution regulated returns to capital

Issue

Board staff proposes to continue to employ the current mechanism for SSM for CDM programs funded through distribution rates. This SSM would apply only to expenditures on the customer-side such as efficiency improvements in the use of electricity, and not to utility-side expenditures such as distribution system improvement projects.

Comments

11. The CLD notes that the deemed return on utility side programs funded through distribution rates will not likely provide a sufficient incentive to invest in CDM programs in preference to needed traditional capital projects.
12. It is understood that any OPA funded capital programs would be excluded from the LDC's rate base and therefore it is appropriate for the OPA to include incentives in the contractual agreement.

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Issue

Board staff recommends that a fully allocated costing methodology be applied to all LDC-delivered CDM activities. Capitalized assets associated with distribution rate funded CDM activities could be included in rate base. Assets purchased with funds from the OPA would not be eligible for inclusion in rate base.

Comments

13. The CLD understands the rationale for this proposal but are concerned about the practical implications of adopting this approach. The implementation may prove to be somewhat more difficult given the timing differences between the signing of OPA contracts and the time of rate rebasing. Commercial contracts with the OPA are expected to cover 3 cost categories: time and materials, administration, and performance bonus. However, it is understood that the administration component of the contract is meant to provide the LDC with a reasonable return, and the performance bonus would be for exceptional performance. This administration component of the contract therefore cannot be linked to the costs to be allocated from the distribution business. For example, if an LDC were to sign a commercial contract with the OPA that accounts for a 10% allocation of an employee's benefits, it would be seeking to recover the other 90% in its next rate case. An LDC cannot seek recompense from the OPA for additional funding if the Board determines that 20% of the employee benefits should have been allocated to the OPA funded program.
14. Furthermore, the CLD notes that initial OPA contracts are contemplated for a 1-year duration only. If an LDC allocates certain costs to CDM through the OPA contracts, thus resulting in lower costs allocated to distribution rates, it is not clear how or when distribution rates would be revised upwards again when the OPA contract expires. This is of particular concern in interim periods when rates are adjusted through the incentive regulation mechanism (IRM), which does not contemplate a rebasing of costs formerly allocated to an OPA funded program.
15. The Minister's July 13, 2006 directive to the OPA did not contemplate that LDCs would be competing against 3rd parties for CDM programs in their service areas. "LDCs would contract to deliver programs funded by an OPA-administrative fund on a non-competitive basis in their territory". Board staff references to "competitive contracts" are assumed to be related to situations in a service area where the incumbent LDC chose not to participate in a particular OPA program and the OPA sought to deliver such program through a third-party (which could include a non-incumbent LDC). In this circumstance, a competitive tendering process would be appropriate.

Issue

Board staff recommends that for OPA funded CDM activities LDCs should be required to provide audited evaluation results when filing LRAM claims.

Comments

16. The CLD supports this recommendation and understand the need to provide evidence of CDM results. The CLD suggests an audit approach that provides assurance within some reasonable level of materiality acceptable to the OPA.

Issue

Staff recommends that LDCs undertake program evaluations, and provide audited results to the Board. In this case, the audit would include the scope identified above as well as the cost effectiveness results as determined by a TRC test analysis. Since this audit is specific to the LDC's unique program, it can also include suggestions for improvements in the program.

Comments

17. The CLD agrees in principle. Providing "suggestions for improvements in the program" would serve to enhance the success of future programs.

Issue

Board staff recommends that the Board limit its reporting requirements for CDM programs funded by the OPA to only the information that the Board needs to assess an LRAM claim, and that the information only be required when such a claim is filed.

Comments

18. The CLD supports this proposal.

Issue

For CDM programs funded through distribution rates, Board staff recommends that the reporting requirements be based on the current annual reporting requirements for third tranche and 2006 funding.

Comments

19. The CLD supports a proposal that minimizes the number of entities to which distributors are required to report information. We would suggest that the OPA be responsible for determining the appropriate quality level of service they expect from the delivery of their funded programs, but that they also consider using the Board's current reporting system to obtain the information.
20. On January 25, 2007, the Chief Compliance Officer for the OEB issued a compliance bulletin. This bulletin indicated that CDM activities that were not funded by distribution rates were undertaken outside of the terms of an LDC's distribution licence. As such, it is unclear why Board staff have proposed that Board service quality indicators would be applicable to OPA funded CDM activities.

If you have any questions regarding this submission please do not hesitate to contact the undersigned or any of those listed below.

Yours truly,

(Original signed by) PAULA CONBOY

Paula Conboy
Director of Regulatory and Government Affairs

cc. Lynne Anderson, Hydro Ottawa Limited
Kathi Litt, Enersource Hydro Mississauga Inc.
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