May 17, 2007

BY EMAIL & BY COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St, Suite 2701
Toronto ON M4P 1E4

Dear Ms. Walli:

Board File No. EB-2007-0031
Review of Electricity Distribution Rate Design
Comments of Energy Probe

Pursuant to the letter from the Board, dated March 30, 2007, providing an opportunity for input into this process, Energy Probe Research Foundation (Energy Probe) is hereby providing its Comments in respect of the staff Discussion Paper released March 30, 2007 entitled *Rate Design for Electricity Distributors: Overview and Scoping*. Three hard copies of the Comments are attached and an electronic copy of this communication in PDF format is being forwarded to your attention.

Should you have any questions or require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh
Case Manager

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EB-2007-0031

Ontario Energy Board

Review of
Electricity Distribution
Rate Design

Energy Probe Research Foundation

◆ Comments on Staff Discussion Paper ◆

Rate Design for Electricity Distributors:
Overview and Scoping

Submitted May 17, 2007

Board Staff Discussion Paper

Rate Design for Electricity Distributors: Overview and Scoping

Comments of Energy Probe Research Foundation

Overview

The following comments are provided on behalf of Energy Probe Research Foundation (Energy Probe) in response to the Board's invitation, by letter dated March 30, 2007, to provide comments on the staff Discussion Paper of March 30, 2007.

The staff Discussion Paper is an excellent guide to a thorny subject; Energy Probe appreciates the opportunity to provide input. While we are able to provide input on some questions raised in the staff paper, we have not responded to all points. As the rate design process progresses, Energy Probe wishes to take advantage of additional opportunities for input and debate.

We have followed the number system used in the staff Discussion Paper.

Chapter 3 – Principles of Rate-making

In discussing principles to apply to rate making, the staff Discussion Paper discusses the tried and true Bonbright eight regulatory principles, but also includes an additional list of five. Energy Probe has comments on these additional items.

1. to encourage conservation

Energy Probe suggests that rate unbundling represents a major gain for transparency and administrative efficiency. The concept of encouraging conservation should apply to each element of the rate, according to the efficiency concerns applicable to that rate element. Distribution rates should be designed to economize distribution costs. Some might argue that distribution rates be distorted to achieve other objectives, such as to discourage usage of commodity power by variablizing all costs. While conservation of commodity electricity is an important objective, it is by no means the only important public policy concern that pertains to the power system and electricity rate making. Variablizing all costs would have the undesirable effect of increasing distribution utility financial risk and would be inefficient.

2. to discourage peak system use

For the same reason that it would be harmful to variablize all costs, it would also be harmful to attach recovery non-peak-related distribution costs to peak charges. Doing so would have the effect of making utility returns excessively vulnerable to weather effects and would reduce the fairness of rates by encouraging cost shifting between customers.

The identification of marginal costs associated with peak distribution system usage, while attractive in theory, may be difficult to achieve in practice. The introduction of smart meters, assuming that the meters are accompanied by smart prices, will provide incentives for customers to avoid usage at times when the distribution system is likely to also face its peak loads. It may not therefore be necessary to implement coincident system peak charges. On the other hand, non-coincident peak charges may remain a useful charge determinant for the recovery of connection-related costs.

3. to promote distributed generation

Distributed generation can enhance overall consumer welfare, but only where its benefits exceed its cost. Expanding distributed generation in Ontario is not in the public interest where its costs exceed its benefit. Efficient and cost-based rates that capture the costs for connection, billing, administration, emergency services, back-up, ancillary services, and other services will promote beneficial distributed generation while promoting overall fairness by eliminating the potential for cost shifting between consumers.

4. to have consistency in distribution rates in Ontario

Energy Probe suggests that while it is appropriate to have a consistent approach for the determination of distribution rates across the province, arbitrarily imposing "postage stamp" rates so that all customers pay the same rate irrespective of the costs of local distribution service, would decrease accountability and cause unfairness. Regional rates might be considered if the efficient costs of providing service in some region were identified as being roughly equivalent. Regional rates might improve the prospects for beneficial mergers.

5. to appropriately address distributors' business risk

Basing rates on cost is one of the most reliable rate principles. Risk to capital represents part of the cost of capital and therefore a cost of doing business. It is therefore appropriate that rates recover costs associated with distributors' business risk. It is also important that rates be designed, as much as reasonably achievable, to mitigate business risk. Mitigation of risk is discussed later in our recommendations on the fixed/variable split.

Chapter 4 – Stages of Rate-making

Section 4.2 Customer Classes: Rate Classification Options

What is the most appropriate basis for determining the service classifications for Ontario distribution customers? Should sub-classifications be maintained? If so, what is the most appropriate method to allocate diversity benefits?

Energy Probe believes that with the advantage of hourly metering data as input for rate setting, aggregation of some current customer classifications might be reasonably undertaken. For example, all general service customers on single phase service might be reclassified as a single class.

Chapter 5 – Rate Design

Section 5.2 Fixed and Variable Rates

What are the principles that should inform the decision on fixed and/or variable rates?

Energy Probe believes that a key principle that belongs in the decisions on the fixed/variable split is protecting the revenue stability of utilities, a key issue area where regulation can influence the movement of the cost of capital downward and thereby minimize long run costs. Further, decisions on the fixed/variable split should be informed by the minimum system approach, with administration and general costs allocated by customer class and customer number and recovered as much as possible through fixed rate components.

Moving rates in the direction of a cost-reflective fixed/variable split would reduce the need for multiple rate classes and thereby simplify the rate structure. For example, Hydro One could eliminate seasonal occupancy rates.

Section 5.4 Cost Model for Generation

Distributed generators should have the opportunity to be paid for the full value of the power they provide to the distribution system. Where a distributed generator contributes ancillary services, transmission loading relief, line loss reductions and/or other services that are beneficial to other consumers, that generator should be fairly compensated.

Section 5.5 Consistency of the Rate Design

How important is consistency of the rate design model across the province? Is one single rate order (or a few regional rate orders) to be used by all distributors a desirable outcome?

Moving toward rate design harmonization would provide multiple benefits. Rates would be simpler and more easily compared between regions. Utility mergers would be simplified by reducing rate harmonization barriers.

Energy Probe believes that the Board should establish clear guidelines for rate harmonization in the event of mergers. Utilities and customers should be able to know the rules in advance of any corporate restructuring. Energy Probe presented its analysis of this issue in greater detail in response to EB 2007-0028 LDC Consolidation, in our submission filed with the Board on April 5, 2007.

Energy Probe does not support pooling of the revenue requirements of more than one distributor. Pooling of revenue requirements would reduce utility transparency and accountability.

Section 5.10 Impact of the Simplified Bill

Given the simplified bill, can a conservation and/or demand management effect be achieved through distribution rate design?

Energy Probe suggests that the objective of rate redesign should be to move in the right direction. Many circumstances, including the current government-mandated simplified bill, may slow progress in getting to the right direction, but circumstances change. Some of the basic rate design questions considered in this process were last considered in the 1980s. Many changes in policy and other circumstances have elapsed since then. It is possible that after this review of distribution rate design is completed, that further review may be a decade or more in the future. If the foundation is laid today for improved rates, the Board can only expect that some benefit may arise, although date of realization of those benefits cannot be foreseen.

Hopefully the simplified bill will be replaced by the smarter bill.

Energy Probe appreciates the opportunity to review and comment on the staff Discussion Paper.

Respectfully submitted at Toronto, Ontario this 17th day of May, 2007.

Thomas Adams