



June 27, 2003

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street
26th Floor
Toronto, ON
M4P 1E4

Attention: Mr. Paul Pudge, Board Secretary

Dear Sir:

**RE: Consumer Security Deposit Policies – RP-2002-0146
Newmarket Hydro Ltd. Submission**

We have reviewed the proposed changes to the Distribution System Code to address consumer security deposits and respectfully offer the following comments and observations.

Our current position:

Up to the end of 2001, we had the ability to recover unpaid electric bills incurred by homeowners and businesses that owned their premises through municipal tax liens. For the past 20 years, we have had a security policy that required:

- A 90-day security deposit from all consumers that were tenants.
- No security from consumers that owned their premises as we had the ability to use tax liens to collect unpaid bills.

The result of this policy has been annual doubtful account losses of less than \$25,000.00 representing 0.3% of total expenses. With the loss of the ability to tax lien for arrears, there is a simple and prudent method of limiting our exposure to non-payment. That is to apply the security requirements we have always employed for tenants to owners as well. This policy is currently contained in our Conditions of Service. We appreciate this approach is not in keeping with the current industry changes, and the negative financial impact it could have on our industrial consumers. Thus, we are currently seeking comments from our largest general service consumers who are owners of their facility on proposed changes to our security deposit requirements in our Conditions of Service. The proposed changes, once finalized will be applied equally to all consumers. Should Board involvement in security arrangements at this time restrict our ability to set what we deem to be a prudent policy, there will be an undesired increase in our doubtful account losses.

Response to RP-2220-0146 Consumer Security Deposit Policies

The impact of change – Consider the outcome:

We would expect the Board to address any increase in exposure to non-payment risk as part of any security policy it may prescribe. If the Consumer Security Deposit Policies as proposed by the Board (the 'Proposed Policies') are less prudent than ones we would otherwise adopt and be prepared to defend, there will be a need to ensure any negative financial impact on us is fully mitigated. We realize this could place upward pressure on the rates we charge to consumers. It begs the question as to why our consumers that represent low risk are left to pay for those who do not.

In any commercial credit arrangement, be it a loan or a credit card, the subscriber has the option to pay within a specified period. In doing so some or all credit charges are avoided. Thus, the consumer has the ability to avoid being burdened with the costs of those who represent payment risk. Creditors have the ability to take any action available to them under law to secure payment. Under all prevailing rate setting regimes in the electric industry, the subscriber (consumer) has no ability to avoid the costs of those who do not pay if doubtful account losses are incorporated into them.

The Proposed Policy does not address future non-payment risk or exposure:

We also find that the Proposed Policies as presented are superficial and do not address consumer non-payment risk and our resulting exposure. In fact, they are detrimental to the best interests of the consumer and the financial well being of Newmarket Hydro Ltd. ('NHL'). There are a number of reasons for this including:

- The Proposed Policy's good payment history does not measure risk of future non-payment:

The definition of good payment history in section 2.4.10 does not measure the risk of non-payment for a given consumer. Any consumer may have a cheque returned for insufficient funds or miss a payment for any number of reasons ranging from a period of restricted cash flow to simple forgetfulness. The consumer's timely payment of all debts as they are due over time is a legitimate measure of the ability to pay. Late payment of accounts and commercial credit ratings are more legitimate measures of credit risk that have been ignored.

- Timing of deposit requirements is counter-intuitive:

The concept of not holding a deposit and then requiring one after bills have gone unpaid as contemplated in Section 2.4.9 is counter-intuitive, onerous and not in the interests of our consumers. To demand a deposit of a consumer that has encountered financial difficulty and unable to pay a utility bill simply exacerbates their situation. It causes financial and, if disconnection of service is imminent, physical distress at a time when the consumer is least able to deal with it. It is obvious that a consumer who cannot pay a single bill will have no available means of paying an amount that represents a multiple of that bill. If the supply of electricity is disconnected to an industrial consumer, there is absolute certainty of this. Without electricity, they have no ability to produce their products to generate earnings. Deposit requests are ideally made when the consumer is in a sound financial position and best able to afford it.

Response to RP-2220-0146 Consumer Security Deposit Policies

- Cycle factors are really credit terms that represent exposure:

The cycle factors in 2.4.16 clearly demonstrate the Board recognizes that NHL is extending 75 days of credit to our consumers based on our monthly billing cycles. We are expected by our suppliers of goods and services to pay within 30 days. These 30 days of credit is a commercial norm. We must pay our electricity supplier, the Independent Market Operator within 45 days of delivery and post full security to guarantee payment.

Some of our largest general service consumers use over \$5,000.00 per day of electricity and non-competitive charges. Under the Proposed Policy, payment for 75 days of consumption at this daily rate would be totally unsecured in many cases. The Board should be extremely wary of requiring us to extend credit terms to consumers that we do not enjoy and they do not generally have access to. Other industry participants could construe this as a consumer subsidy by NHL. It is not in keeping with maintaining a financially viable electricity industry.

- Future Non-payment risk is not a function of consumption:

Section 2.4.9 and the supporting Working Group discussion suggests holding deposits for different terms depending on consumption. This implies that future non-payment risk is a function of consumption. This notion is unfounded. Indeed, the following points would suggest that there might be no correlation at all:

1. As the consumption of electricity in the general service class reduces, the number of consumers increases dramatically. The product of the number of consumers times the average consumer consumption, which is a legitimate measure of risk exposure, has been ignored.
2. As the number of consumers increases, simple probability theory states that the likelihood of non-payment also increases. While the submitter does not have the resources to determine the increase in probability, it is likely non-linear as small businesses tend to be relatively short-lived compared to large conglomerates.
3. Large industrial consumers served by NHL generally own their facility. This represents a very significant investment that they are incented to protect. They employ very prudent business practices and constantly strive for financial stability. Nonetheless, the financial exposure they represent is very significant.

While financial exposure increases with consumption, the probability of non-payment may not. Both factors must be considered.

- Canadian insolvency legislation that greatly increases future non-payment risk has been ignored:

Legislation such as *The Companies' Creditors Arrangement Act* ('CCAA') is a significant factor in non-payment risk. Corporate protection under this act severely restricts our ability to recover amounts owing prior to protection and secure payment

Response to RP-2220-0146 Consumer Security Deposit Policies

of accounts going forward. Protection under this act is extremely difficult, if not impossible to foresee. A prudent risk management policy would take this into account. A minimum response is to limit exposure by limiting credit extended to a commercially accepted norm. Extending 75 or more days credit to businesses is simply not prudent. Under CCAA for example, a deposit can be used as a set-off against monies owing. The Proposed Policies make no acknowledgement of this extremely significant payment risk that exists in the entire general service class.

➤ **Future non-payment risk differs between our residential and general service classes**

Residential consumers, for the most part, have very stable payment habits, be they good or bad. Their credit history affects events in their day-to-day lives from their ability to purchase a home or clothing to taking a vacation. As such, they are continually reminded of the need to pay their debts in a timely manner. The good payment history, if coupled with regular but infrequent credit checks represents a reasonable measure of non-payment risk. The 75-day average consumer exposure is, in the case of NHL, \$300.00. This exposure is relatively small. Thus, if the measure is inadequate, there is ample time to detect a trend in non-payment and implement corrective actions before we incur significant financial losses.

This is not the case for larger general service consumers. Legislation such as CCAA and the fact that the business owners have no personal liability for outstanding electricity bills makes payment stability impossible to predict. The financial exposure is much more significant than the residential class. Indeed, non-payment by our largest general service class consumer can place the company in a financial crisis. Limiting credit extended, more stringent payment history and commercial credit rating criteria are essential to limit exposure.

We are addressing changes in our security requirements:

NHL has expended significant time and resources to research this issue and prepare proposed changes to our Conditions of Service respecting security requirements with our general service consumers. A copy of the PowerPoint presentation describing the proposed changes is attached as Appendix A to this submission. We would be pleased to present it to the Board and/or Board staff for their review and comments.

Meetings were held on June 17, 19, and 20, 2003 with most of our largest general service consumers to discuss the draft policy. This proceeding by the Board was fully disclosed to all attendees. The results are aggregated in Appendix B attached. We will be providing updates to Appendix B as our consumers inform us of the results of their deliberations.

These consumers represent a broad spectrum of industry from automotive, food processing, and medical supply to property management and recreational facilities. They are accepting this policy even with the full knowledge that the Board is considering the issue. In each of the meetings, there was a stated desire to have NHL pursue reinstatement of tax liens to secure payment. Of the 23 consumers we met with, more than half made this request. We encourage the Board to make this recommendation to the Government.

Response to RP-2220-0146 Consumer Security Deposit Policies

We are aggressively pursuing all losses that affect our consumers:

Consumer theft of power also affects the rates we charge. Together with the civil authorities and our neighbouring electric distributors in York Region we have made effective efforts to detect and close marijuana grow houses that steal electricity. The result is recovery of over \$250,000.00 in the last three years. A less than prudent policy to protect against non-payment risk could unjustly erase these gains.

Moratoriums on disconnection create unlimited exposure and skew risk measures:

For the first time in the history of Ontario's electric industry, a moratorium on disconnection as a means of bill collection was imposed in the fall of 2002. Although it ended in the spring of 2003, there could very well be others declared in the future. The results of this action for all LDCs including NHL in terms of late payment and non-payment are widely known. Arrears and non-payment exposure increased dramatically. The good payment history as defined was rendered ineffective as normally good-paying consumers simply took a self-declared payment holiday. We were left in a position of unlimited exposure for those consumers with no deposit. Post-moratorium, many consumers have unsatisfactory payment histories that do not in any way measure their ability to pay.

Security policy administration has always been self-funding:

Interest paid on cash deposits of less than prime rate has always been our norm. NHL does not receive prime rate on cash deposits in our bank savings account, or any other guaranteed investment vehicle available to us. We use the difference between what we receive and what we pay to fund the administration of these deposits. This is fair and equitable as those who are required to pay a deposit and choose to do so in cash pay for its administration. Those who don't post cash or are not required to post security pay only the costs associated with their type of security.

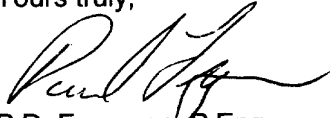
What mechanism will be employed to measure and allow for recovery of these costs should the Proposed Policy be enacted? At the present time, NHL receives prime rate less 1.75% on bank deposits. Payment of prime rate on cash deposits held would cost us \$43,000.00 annually relative to the bank savings rate we receive. Relative to our existing Conditions of Service, the cost is \$81,000.00 annually. Here again, the Proposed Policy is requiring us to offer better terms to our consumers than they would otherwise enjoy in a guaranteed investment. Indeed, cash deposits that yield interest at the prime rate will make them the investment of choice for all consumers.

The Board should be very cautious of burdening us with these additional costs at a time when it has no rate setting authority to grant relief. If security policy symmetry with the natural gas and other industries is desired as suggested in the discussion paper of September 2002 on this issue, fair and reasonable commercial credit practices must be equally considered. It may well be that the security policies of other industries being considered in the symmetry equation are too lax and not in the best interests of the good-paying consumer.

Response to RP-2220-0146 Consumer Security Deposit Policies

While we do not object to a written hearing and understand its protocol, we offer to answer any questions the Board may have on our submission. As mentioned previously, we would be pleased to present our proposed Conditions of Service changes as we have to our largest consumers.

Yours truly,



P.D. Ferguson, P.Eng.
President, Newmarket Hydro Ltd.

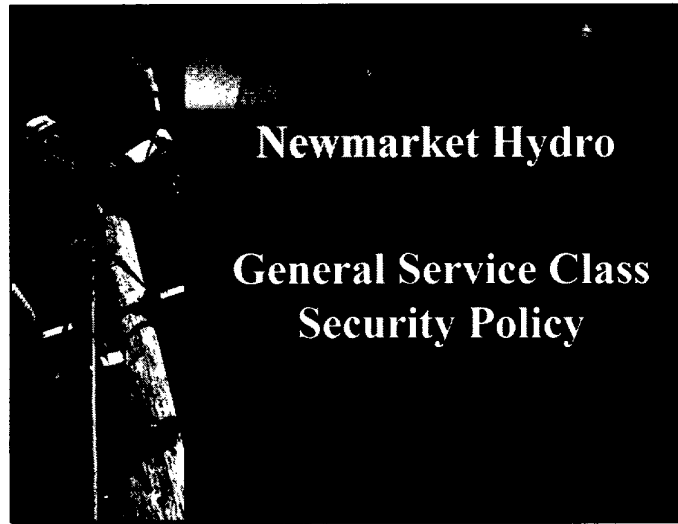
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**Appendix A
NHL Draft Security Policy**

General Service PowerPoint Presentation

Slide 1



Slide 2

Billing for Electricity

- **On average, Newmarket Hydro issues bills for electricity consumed every 30 days**
 - On average, Customer meter is read every 30 days
 - After the meter is read, 30 days of consumption is calculated
 - Consumption cannot be priced until the market price of electricity is sent from the Independent Electricity Market Operator (IMO)
 - Market price is received 10 days after Newmarket Hydro has calculated the Customer's consumption
 - Bill is then priced, printed and mailed

Appendix A – General Service PowerPoint Presentation

Slide 3

Bill Payment Terms

- **Payment of the bill is due 16 days after it is printed.**
- **Collection procedures can be started 14 days after the due date.**
- **Payments (cheques, bank payments) can take up to two weeks to clear financial institutions.**

Slide 4

Billing & Payment Timeline

Day	Billing/Payment Activity
1	Meter is read. End of previous bill consumption period, start of current bill consumption period.
30	Meter is read. End of current bill consumption period.
40	Price of electricity received from the IMO. Bill is priced, printed and mailed.
45	Newmarket Hydro pays the IMO for all electricity consumed by its Customers up to Day 30.
56	Payment of the bill is due from Customer.
70	Collection procedures for unpaid bills can be started.
84	Final clearance or refusal of payments made up to Day 70.

Appendix A – General Service PowerPoint Presentation

Slide 5

**Newmarket Hydro
Observations on Security**

- **Between meter readings, Customer is continuing to consume electricity**
 - Large General Service Customers consume between \$500.00 and \$8,000.00 daily
- **We are extending up to 90 days credit to all Customers.**
- **We must pay the IMO for the monthly electricity consumed by our Customers within 15 days, regardless of whether the Customer pays us or not.**
- **We have historical 'doubtful account' losses of less than \$25,000 annually (Less than 0.3% of expenses)**

Slide 6

**Newmarket Hydro
Observations on Security**

- **Doubtful account losses are recovered in rates**
 - If our losses go up, Customers' rates go up. "We all pay."
- **Prior to Deregulation, we could tax lien property**
 - Business' that owned their facility were not required to post security
 - Business' that were tenants have always posted security with Newmarket Hydro (practice for over 20 years)

Appendix A – General Service PowerPoint Presentation

Slide 7

**Customer Security Considerations
Bill Payment & Terms**

- **Good payment history and credit worthiness scoring for General Service Customers is not sufficient security by itself**
 - **CCAA protection can be very swift and difficult to foresee.**
 - **Electricity bill payment is minimum 'due net 60 days', maximum 'due net 90 days'**
 - **Cheque clearance time through financial institutions can be significant**

Slide 8

Residential Class Security

- **Residential Customer**
 - **90 day average exposure of \$300.00**
 - **Pre De-regulation**
 - **No owner required to post security because of ability to tax lien**
 - **All tenants post 90 day security**
 - **Post De-regulation**
 - **Beginning in 2000, all Residential Class Customers make security arrangements**
 - » **90-Day deposit with no payment history or credit score**
 - » **No deposit with excellent payment history or credit score**

Appendix A – General Service PowerPoint Presentation

Slide 9

General Service Security

- **General Service Customer**
 - 90 day exposure from \$5,000.00 to \$750,000.00
- **Pre De-regulation**
 - No owner required to post security because of ability to tax lien
 - All business' that are tenants post 90 day security
- **Post De-regulation**
 - From 2000 to 2003, legacy credit practices used for existing Customers
 - Beginning 2000, all new Customers make security arrangements

Slide 10

Three Dominant Issues

- **Current Bill Not Due for 60 Days**
 - Instant, continuous and non-discretionary supply to Customer up to initiation of collection procedures
 - Payment of account prior to due date reduces exposure.
- **Payment Clearance Time**
 - Electronic payment of bill reduces exposure from 90 days to 60 days
 - Ensures payment on Due Date
 - Eliminates financial institution clearance time
- **Recognition of Payment History and Credit Score**
 - Acceptable when payment terms are 'Due net 30 days' or better.

Appendix A – General Service PowerPoint Presentation

Slide 11

Payment Risk Policy

General Service Customers with an excellent payment history and credit score will be extended 'Due net 45 days' credit terms.

General Service Customers with a satisfactory payment history and credit score will be extended 'Due net 15 days' credit terms.

Others will be C.O.D.

Security amounts will be based on 75 days of consumption.

Slide 12

Security Rating

- **Credit Score:**
 - Less than 10 Excellent
 - 10 to 19 Satisfactory
 - 20 or more Elevated payment risk
- **Payment History:**
 - No disconnect notices in past 5 years
 - No more than 1 reminder notice annually
- **Forms of Security:**
 - Cash
 - Letter of Credit (Preferred)

Appendix A – General Service PowerPoint Presentation

Slide 13

General Service Security Options
Credit Score Greater Than 20 *OR*
Payment History Requirements Not Met
75-Day Deposit Requirement

Options:

- 1. Electronic Payments**
 - Eliminates payment clearance time
 - Reduces deposit requirement by 15 days
- 2. Pay one 30-Day accelerating billing and equal payments every 30 days thereafter**
 - Reduces deposit requirement by 30 days
 - Reduction in deposit by 45 days if combined with (1)

Slide 14

Security Options
Credit Score Between 10 and 19
Payment History Requirements Met
60-Day Deposit Requirement

Options:

- 1. Electronic Payments**
 - Reduces deposit requirement by 15 days
- 2. Pay one 30 day accelerating billing and equal payments every 30 days thereafter.**
 - Reduces deposit requirement by 30 days
 - Reduction in deposit requirement by 45 days if combined with (1) above
- 3. Frequent Payments – equal bi-monthly payments**
 - Reduces deposit requirement by 15 days
 - Eliminates deposit if combined with (1) and (2) above

Appendix A – General Service PowerPoint Presentation

Slide 15

Security Options
Credit Agency Score Less Than 10
Payment History Requirements Met

45-Day Deposit Requirement

Options:

- 1. Electronic Payments**
 - Reduces deposit requirement by 15 days
- 2. Pay one 30 day accelerating billing and equal payments every 30 days thereafter.**
 - Reduces deposit requirement by 30 days
 - Eliminates deposit requirement if combined with (1) above

Appendix B

NHL Draft Security Policy

Presentation Results as of June 26, 2003

Customer's Average Monthly Bill	Consumers In Attendance	Policy Acceptance & Option	Under Consideration	Rejection of Policy
\$5,000 to \$9,999	6	0 – Option 1 0 – Option 2 0 – Option 3 2 – Option 4 0 – Option 5	4	0
\$10,000 to \$20,000	5	0 – Option 1 0 – Option 2 0 – Option 3 5 – Option 4 0 – Option 5	0	0
\$20,000 to \$49,999	7	0 – Option 1 1 – Option 2 0 – Option 3 1 – Option 4 0 – Option 5	5	0
More than \$50,000	5	0 – Option 1 0 – Option 2 1 – Option 3 1 – Option 4 0 – Option 5	3	0
Totals	23	11	12	0

Options:

1. Do nothing and pay the required deposit in cash or Letter of Credit
2. Pre-authorized debit or electronic funds transfer bill payment
3. Accelerated payment and equal billing
4. (2) and (3) above combined
5. (2) and (3) above combined with bi-monthly equal payments