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July 9, 2003

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

Re: Board File No. RP-2002-0146 Consumer Security Deposit Policies

This is in reference to the Board's Notice of Proceeding to amend the Distribution System Code (DSC) for consumer security deposits with consequential changes to the Retail Settlement Code (RSC). Hydro Ottawa is interested in participating in this proceeding and provides the following comments.

Section 7.2.3 of the RSC

Hydro Ottawa supports the proposal to consolidate consumer security deposit issues within the Distribution System Code.

Section 1.2

The acronym of SSS is used in the definition of a "competitive retailer". This has not yet been defined in the Distribution System Code so a definition should be added.

Within Hydro Ottawa's collection procedures there are both disconnect trips and collect trips each of which are undertaken if the consumer has not demonstrated a "good payment history". The definition proposed implies that all collect trips are also disconnect trips, but this is not the case. Therefore, the definition should be amended as follows:

"disconnect/collect trip" is a visit to a consumer's premises by an employee or agent of the distributor to demand payment of an outstanding amount ~~and~~ or to shut off distribution of electricity to the consumer failing payment.

Section 1.7

Hydro Ottawa's customer information system is not capable of automatically tracking the "good payment history" information in a manner that is proposed. As such a manual work around system would need to be developed. Three months would be a very short timeframe to put this in place. There are also policies and practices to be written, staff training to prepare and coordinate and the re-issuance of the Conditions of Service. Since this could not be classified as an urgent issue, providing distributors with sufficient lead-time to properly manage any changes should be acceptable. Hydro Ottawa proposes 6 months.

Section 2.4.6.2

This section states that: *“a distributor may use any risk mitigation options available under law to manage consumer non-payment risk”*. This is exactly what Hydro Ottawa has already done in developing its current consumer security deposit policy. Hydro Ottawa’s policies were developed using decades of experience in managing collections issues and balancing this with the goal of providing excellent customer service. While Hydro Ottawa is fully in support of the wording proposed for Section 2.4.6.2, it is in direct conflict with sections 2.4.9, 2.4.10, 2.4.11 etc. which severely restrict a distributor’s ability to manage that risk.

Section 2.4.9

Hydro Ottawa has always had a policy of waiving a security deposit for a residential customer that can demonstrate a good payment history from another hydro company. This is because past payment history for a residential customer is often a reliable measure of future payment performance. However this is not true for commercial customers. A good payment record is just one factor in considering risk. Success in a previous jurisdiction is an unreliable measure of success in a new location and a changing economic environment can have a significant impact on a commercial customer’s ability to pay, regardless of good intentions. Experience with the bad debts left when a commercial customer initiates bankruptcy protection resulted in Hydro Ottawa’s current policy of collecting security deposits from all commercial customers and holding these for as long as the customer’s account is active. This is consistent with the prudential requirements issued by the IMO for electricity market participants. This practice is also consistent with the proposed section 2.4.6.2 that permits distributors to use “any risk mitigation options”.

This section, as it is currently written, would not permit distributors to use credit ratings as a measure of risk for commercial customers in a similar way as the IMO. It is the business of rating agencies to analyze the market risk and it is done consistently across companies in different industries so the result would be non-discriminatory. This would also result in a similar measure of risk across the province for companies that operate in multiple jurisdictions. Furthermore, the use of credit ratings would provide greater integration between the wholesale and retail markets, a goal that the IMO has been promoting.

Another factor that is seldom considered with respect to security deposits is the ability of a distributor to be far more flexible in agreeing to payment arrangements for consumers with outstanding amounts if a deposit is in place. This can reduce the number of consumers that will be disconnected for non-payment. Without a deposit on account the distributor will need to mitigate its risk by proceeding to disconnect a service for non-payment rather than extending the time for payment.

Section 2.4.10

Hydro Ottawa is very concerned about the Board’s proposal to prescribe what is deemed to be a “good payment history”. This assumes that collections practices are consistent from distributor to distributor, which is not the case. The definition of a disconnection notice and the stage of the collection process in which it is sent can be very different between distributors. This notice could be sent as soon as the amount is past due or following a reminder notice. If a distributor’s collections practices are such that a reminder notice is sent before a disconnect notice, or if the disconnect notice is hand delivered during a “collect trip”, then one such notice should be sufficient to negate a good payment history record. However not all distributors issue reminder notices. Hydro Ottawa has tailored its measure of “good payment history” for residential customers based on its own collections processes, as have other

distributors. It is strongly recommended that this section be revised to indicate that the distributor will set out its own measure of good payment history, and that this will be documented in its conditions of service.

Section 2.4.11

Once again, good payment history from a previous jurisdiction is an unreliable measure of payment risk for commercial customers. This section should be revised so that it only applies to residential customers. Furthermore, Hydro Ottawa has always accepted information from electricity companies in other provinces as evidence of good payment history. This is particularly important given our proximity to the Québec border.

Section 2.4.12

Hydro Ottawa currently sets the deposit amount for a residential customer based on the best estimate of consumption for that particular customer during the highest consumption month. This is the most accurate measure of the risk that a distributor undertakes with that customer. Using a class average, while simpler, is not fair to low volume consumers and is not a fair reflection of risk for customers with higher than average consumption.

Section 2.4.13

Setting deposits based on an average monthly load does not adequately mitigate a distributor's risk. The deposit should be based on the distributor's maximum exposure therefore the deposit should be based on the "consumer's peak month load". This is the same way that prudentials are set for retailers and market participants.

Section 2.4.14

This section states that 4.3 cents should be used to determine the deposit requirements for low volume consumers but, with the possibility of new contracts being placed at new rates, the wording should include "*unless the customer has contracted for a higher rate in a retail contract after December 9, 2002.*"

Section 2.4.15

The Board has indicated that if a distributor has not been prudent with respect to the collection of security deposit it could put at risk its recovery of commodity costs. If a distributor reduced a security deposit as permitted under this section, would this be considered imprudent by the Board?

Section 2.4.17

As discussed under section 2.4.12 and 2.4.13 deposits should always be based on the maximum exposure therefore this section would be redundant.

Section 2.4.19

Hydro Ottawa currently permits a deposit to be paid in equal installments over a 3-month period. This practice has worked well and is highly recommended instead of the 4-month period proposed in this section. If the period is extended any further a distributor can be in the situation of initiating collection action for non-payment prior to having collected the full deposit. It is highly important that distributor be able to stipulate the size of the installments permitted so that a consumer could not propose to pay only a small amount upfront with a promise to

pay the remaining portion at the end of the installment period. As such, section 2.4.20 should be revised to state that: *“A distributor shall permit the consumer to provide a security deposit in installments as stipulated by the distributor.”*

Section 2.4.21

Hydro Ottawa is strongly opposed to the proposal set out in this section. Paying interest at the Prime Business Rate would result in distributors paying out interest at a rate far higher than a consumer could expect to attain elsewhere for a fully secured short-term investment of small dollar quantities. Distributors would lose money on all deposits that are held since the distributor could not hope to achieve that same interest rate on a short-term investment. Hydro Ottawa currently pays interest at the amount that a customer would earn on money in a daily interest savings account. This ensures that only the interest that Hydro Ottawa earns on the money is returned to the consumer. Furthermore, the administrative complications in trying to pay out the interest annually would make it so costly to manage deposits that it may no longer be worth collecting them.

The IMO offset of prudential obligation, which is provided to distributors for deposits held from consumers, assumes that the deposits are liquid and can be accessed very quickly. This means that the deposits must be in cash or near cash. Therefore the return that a distributor can earn on these deposits is far less than the prime rate. The customer can leave and request a deposit to be applied or refunded at anytime and this uncertainty must be reflected in reduced interest rates for the customer.

Section 2.4.22

It is seldom recognized that a distributor incurs significant administrative costs to collect and manage deposits. In developing any security deposit policy these administrative costs are weighed against the financial risks to ensure that the program is cost effective. It is the role of the distributor to determine these issues. Once the costs have been incurred to collect the deposit it must be held for a sufficient length of time for the distributor to satisfy itself that the risk has been minimized. For residential customers Hydro Ottawa has determined that this is 3 years. However for commercial customers, Hydro Ottawa’s experience in dealing with bankruptcies, and the resultant bad debts, is that the risk is never truly minimized because economic and environmental factors play such a large role in the success of a commercial venture. Hydro Ottawa needs to be able to use all tools at its disposal to minimize this risk and the most important of these is maintaining a deposit on account for as long as that commercial customer is in operation.

If the Board’s proposed security deposit policies were adopted by the IMO, most market participants including Hydro Ottawa would post no prudential requirements at all. Yet the IMO has assessed that this would pose too much risk to the electricity market. Hydro Ottawa is simply applying the same approach.

Section 2.4.23

This section seems to contradict section 2.4.22. Under section 2.4.22 deposits are only returned upon a customer’s request, but under this section it implies that during the annual review the entire amount of the security deposit may have to be returned. The total section should be removed since the amount of the deposit is already prescribed in previous sections.

Section 2.4.27

Seasonal customers can be classified as either residential or general service. For instance, Hydro Ottawa would classify a Christmas tree lot as general service. Therefore this section should be revised to say that: *“a seasonal consumer, who is not otherwise classified as general service, shall be deemed to be a residential consumer.”*

Concluding Comments

Hydro Ottawa participated in this exercise with one driving concern and that was to gain an understanding on how the Board would be evaluating a distributor’s “prudence” with respect to commodity risk. This is based on the letter sent to all distributors on December 6, 2001 from Paul Pudge which stated that: *“it is not intended that the distributor take on business risk related to the commodity costs because this would affect the distributor’s neutrality with respect to consumers’ choice of suppliers.”* And further that: *“distributors are not intended to be held generally accountable, or at risk, for uncollected commodity costs from consumers or retailers. A distributor may be held responsible for commodity costs if it were found to have been imprudent, for example, it had failed to follow its security deposit policies.”* However, this was the one issue that was never addressed in this proceeding and distributors are still left pondering this issue.

In conclusion, distributors like Hydro Ottawa have been managing collections issues for decades and have developed security deposit policies based on extensive experience in balancing financial risk with the objective of provided the best services to customers. Hydro Ottawa feels that it is in the best position to set the policies and practices based on local conditions. The proposed changes to the Distribution System Code go too far in prescribing how a distributor is to manage its operations.

Further questions can be directed to me using the contact information shown below.

Yours truly,

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