

Draft Meeting Notes - #2
Consumer Security Deposit Working Group
Tuesday, October 1, 2002
9:30 a.m. - 3:00 p.m.

Roy O'Brien (Canadian Cable Television Assoc.)
Melanie Currie (Canadian Federation of Independent Business)
Julie Girvan (Consumers Association of Canada)
Tony Paul (Electricity Distributors Association)
Rita Ronca (Enersource Hydro Mississauga)
Laurie Elliot (Hydro Ottawa)
Brenda Bracken (Hydro One)
Dawn Case (Milton Chamber of Commerce)
Robert Clarke (Milton Chamber of Commerce)
Karen Fawcett (London Hydro)

Mary Jo Corkum (Milton Hydro)
Don Thorne (Milton Hydro)
John Savage (Ministry of Energy [Observer])
John Armstrong (Rogers Cable)
Frank Fabiano (St. Catharines Hydro)
Mary-Ellen Viger (Toronto Hydro)
Judy Rosebrugh (Wellington North Power)
Chris Cincar (Ontario Energy Board)
Martin Davies (Ontario Energy Board)
Paula Conboy (Ontario Energy Board)

NOTES OF MEETING

1) Review of notes from September 23, 2002 meeting

The following edits were suggested to the notes:

- C 2nd bullet under LDC Issues should read, "Aspects of the current market design are flawed and contribute to security deposit issues"
- C 5th bullet under LDC Issues should read "Claims of insufficient bad debt allowance for some LDCs. Is historical data (1999) appropriate under different rules going forward?"
- C An additional bullet suggested under LDC Issues to highlight that LDCs need to have clear guidance/definition on what constitutes "prudence" or "due diligence" in the view of the Board when determining whether to allow recovery through rates of bad debts in excess of allowance already factored into distribution rates.
- C 6th bullet under Other Matters Discussed, should read, "It was estimated that about 30-40% of LDC load is related to interval-metered customers."

There were further discussions stemming from the review of Meeting Notes:

- C IMO has the ability disconnect for non-payment of prudentials (wholesale market participant (WMP) dumped into retail market), but unclear if LDCs able to disconnect for security non-payment.
- C If distributor consolidated billing, LDC on the hook for full amount.
- C Good payment history not taken into account by Collus in security deposit determination.

- C Collus uses 6.5 cents for security deposit calculations. Only logical since IMO uses for wholesale MPs and LDCs use for calculation of retailer prudentials.

2) Collingwood Utility Services Presentation – (Darius Vaiciunas)

Darius walked working group through a Powerpoint presentation describing the process Collingwood Utility Services went through in revising their deposit policy for changing market conditions, and the response received from their largest interval metered customers. Powerpoint presentation attached.

Summary of Presentation:

- C Policy focused along two dimensions: *risk and exposure*.
- C Customer segments assessed on each dimension. For example, large commercial customers deemed to be high risk and high exposure.
- C Initially planned to take security at 2.5 times monthly bill from all large interval metered customers
- C Risk profile ... load profile (e.g., schools not required to pay security deposits).
- C 10 largest customers were consulted and came back with alternate suggestion that provided customer with an option to posting hard security while at the same time providing utility an early warning of potential default and reducing exposure.
- C Option consisted of providing interval-metered customers the ability to view (on web site) and pay weekly the charges related to commodity, DRC and WMSC. This reduces the amount of exposure utility has to the customer and also provides utility with an early warning of potential payment problems and default. At the same time, utility takes parental guarantee letter to cover 30 days exposure. No checking of parental company credit rating.
- C Some large customers did not take the advancement payment option and were, thus, required to pay the security deposit.
- C Weekly payments are monitored with the bank by utility staff.
- C Offering this alternative has been accepted by BoD, shareholders and customers.
- C Advance payment option forcing customers to better understand the new market.

Participants discussed the following additional points during the presentation:

- C There are incremental costs to billing and monitoring payments weekly that need to be recognized.
- C *Can LDCs legally disconnect for non-payment of security deposits? View of the LDCs is “yes” if the security is identified as a condition of service or of continued service. Customer participants agreed that LDCs would not be*

- able to collect security deposits if they couldn't disconnect for non-payment of them.
- C *Should Retailers share in consumer non-payment risk for their enrolled customers whether or not distributor or retailer billed?*
 - C Both London and St. Catharines LDCs are doing advance billing of some larger customers as an alternative to taking deposits to cover 2.5 months exposure.
 - C At the end of the day, would OEB view Collingwood credit management approach to be "prudent" and therefore allow recovery of default amounts not covered by security?
 - C It was clarified that this option was not a form of prepayment. Instead, it was "pay-as-you-go" as the customer always owes Collus \$'s.
 - C Deposit is a balance sheet item, while "pay-as-you-go" is a P&L (profit & loss) item. In other words, a deposit and "pay-as-you-go" are similar in that the customer provides the LDC with cash before the invoice is received in both cases. However, a deposit is not an expense, while "pay-as-you-go" is treated as an expense.
 - C Concern that this process will only result in Guidelines but need a clearly defined policy.
 - C If all defaults included in bad debts allowance, how fit into PBR?
 - C If all defaults included in bad debts allowance, defaulting customers will have, at least, contributed to some degree to a "slush fund".
 - C If recovery in rates, who pays (e.g., within customer class)? Objective should not be to cross-subsidize non-payers of a security deposit.
 - C Board made a statement with Brampton Hydro decision.
 - C Where do you draw the line between automatic recovery in rates and determining prudence? Responsibility to protect customers.

3) Discussion of Guiding Principles

- a) *Symmetry*: There should be some symmetry (but not necessarily perfect symmetry) between LDCs' security deposit practices. Given the range of customer, community, shareholder and political circumstances faced by LDCs, it was generally agreed that the only way to bring about this symmetry is by OEB providing deposit policy standards and allowing LDCs some flexibility in application.
- b) Symmetry with wholesale market might be desirable. Not necessary to have symmetry with natural gas industry which is quite different.
- c) The issue of the potential for cross subsidization arose within the context of who should bear the burden of a default. Should it be borne by:
 - LDCs shareholders?
 - by all customers via recovery through distribution rates?

- by customer class or segment where the default occurred via recovery through distribution rates charged to that class/segment?
 - by only the segment of customers within a customer class that did not post a security deposit?
 - by retailers and generators who are profit-motivated entities?
 - by extension of the wholesale market residual risk pool to include the retail market?
- d) Risk should follow profit/benefit (i.e., retailers and generators that profit should assume some of the risk).
- e) Policy standard should address:
- alternatives to cash deposits
 - retention periods
 - interest on cash deposits, etc.
- (The above are all examples of possible “minimum requirements”. It was decided to complete the discussion of “principles” and focus on “minimum requirements” at next meeting).
- f) Take a business approach to risk management, i.e. consider some allowance for good credit/payment history and return of security after a period of good performance.
- g) *Increased consistency amongst LDCs:* At the same time, all LDCs are different and face different risks.

4) **Brainstorming: Potential Options/Solutions:**

- C OEB staff obtained and circulated a copy of Great Lakes Power deposit policy (as per request at previous meeting). The intention was to investigate how the private utilities had managed, in the past, without access to the tax roll. However, discussions with some of these private utilities found that they (like many LDCs) had simply become more vigorous in enforcing their policies (i.e., not being so lenient) since the market opened to competition.
- C Retailers should share in the risk of default for their enrolled customers, i.e. they should not be paid 100% by LDCs and the LDCs be required to hold all the risk.
- C 1999 level of bad debt allowance is factored into current LDC distribution rates, but this might not be a “typical” or “average” level of bad debt for a particular LDC and there needs to be a means for LDCs to recover default amounts in excess of this allowance level, provided they have demonstrated “prudent” credit and collections management.
- C Suggestions for possible recovery included:
- Via relevant *Retail Settlements Variance Accounts*, i.e. since bill components are unbundled, bad debt write-offs should be booked to the relevant variance account (e.g., commodity to RSVA Power, etc.).

- Via creation of a *bad debts reserve fund* to which all customers would contribute through their distribution rates or a special surcharge on their bills. If the reserve fund became too large, it would be passed back to customers via a reduction in their distribution rates or one-time rebate.
 - Via transfer of all (or some, based on a threshold) of the bad debt in excess of the allowance to the *wholesale market residual risk pool*.
 - Via *line losses* since already includes bad debts (but is not currently high enough due to new risks).
- C Need to ensure appropriate balance between level of bad debt that is recovered through distribution rates and appropriate risk mitigation strategies taken by the utilities.
- C LDCs need to better understand and quantify their exposures/risks in the new market.
- C OEB should determine whether it wants LDCs to take on risks of the wholesale market or to be merely pass-through entities.
- C WMPs who default have their default amounts flow into the wholesale market residual risk pool where they are recovered through all wholesale market participants (and through WMS charges to retail customers). Suggestion made to treat non-WMP default in the same manner, i.e. recovery through the wholesale market residual risk pool provided LDC has exercised “prudence/due diligence”.
- C Should be a seamless boundary between the wholesale and retail markets.
- C If LDC bad debt allowance exceeds actual bad debts in a given year, give the excess back to customers through distribution rates charged the following year and vice versa.
- C Net bad debts, in excess of allowance, taken off LDC’s IMO bill if prudence has been established.
- C If Retailers become WMP, then they will share in the residual risk pool, but it does not make retailers directly responsible for default of their enrolled customers who are billed by LDCs (nor should they be responsible in the opinion of some LDCs).
- C Load limiters instead of outright disconnection for residential customers in the winter.

5) Implications

- i) OEB must establish standard deposit policy/guidelines to provide consistency across the province
- ii) OEB must provide guidance to LDCs on what constitutes “prudence” or “due diligence” in credit and collections management. If prudence not established, the shareholder should “eat” the loss out of their return.

- iii) Suggesting that OEB must be prescriptive in terms of policies and what is prudent. At the same time, LDCs stating all LDCs are different and face different risks. How does OEB balance being prescriptive and flexible at the same time?
- iv) If all defaults go into bad debts allowance, all allowances for bad debts need to be removed from current rates.
- v) Extension of the wholesale market residual risk pool to include the retail market would require Market Rule changes. OEB cannot change Market Rules on own motion. Proposed changes must first go to IMO via a stakeholder or market participant. If IMO rejects, then option to appeal to OEB.
- vi) If simply include in residual risk pool or bad debts allowance, what incentive is there for LDCs to be prudent and make necessary efforts to collect? This is where prescriptive definition of prudence is applicable. Still, how can OEB check that LDCs are making necessary efforts to collect?

6) **Next Meeting**

Wednesday, October 9, 2002
11:00 a.m. to 4:30 p.m.
OEB offices
25th floor, North Hearing Room

Notes prepared by Brenda Bracken (Hydro One Networks), with assistance from Chris Cincar (OEB).