

1 **Ontario Energy Board (Board Staff) INTERROGATORY #9 (Prefiled Evidence)**

2
3 **Interrogatory**

4
5 At page 5 and elsewhere, Networks refers to an obligation to plan for future growth and
6 an obligation to serve customers within its service territory.

7
8 a) Before the *Energy Competition Act, 1998*, from where did this obligation arise? Was
9 this obligation consistent with the provisions of the former legislation referred to at pages
10 18 and in Appendix A that allowed municipalities to purchase Ontario Hydro assets?

11
12 b) Is there currently an obligation to connect future customers within a utility's service
13 territory?

14
15 **Response**

16
17 (a) and (b):

18
19 The obligations to plan for growth and serve customers, both before and since *Energy*
20 *Competition Act, 1998* ("ECA"), flow from a statutory and common law framework that
21 has established and maintained discrete distribution service territories. This interrogatory
22 response provides an overview of the obligations in Ontario, addresses the foundation of
23 these obligations in the current and previous legislative framework, and assesses the
24 significance of these obligations not being found to reside with the incumbent LDC.

25
26 **Obligation to Plan and Serve Prior to and Since the ECA, 1998**

27
28 Since 1998, the *Electricity Act*, ("EA"), the *Ontario Energy Board Act* ("OEB Act") and
29 the *Distribution System Code* ("DSC") established under the OEB Act provide the
30 statutory foundation. While section 70(6) of the OEB Act says that the service territory of
31 LDCs is "non-exclusive", the obligations imposed upon an LDC by both statutes, the
32 DSC and the LDC's licence require that the LDC has the obligation to plan for and to
33 serve customers within its entire licensed territory until such time as an amendment is
34 made to its licensed territory. Prior to the EA, the obligations to plan for growth and serve
35 customers within a distribution utility's territory stemmed from the common law
36 obligation and three statutes, namely the *Power Corporation Act [Power Commission Act*
37 *until 1973]* ("PCA"), the *Public Utilities Act* ("PUA") and the *Municipal Franchises Act*
38 ("MFA").

39
40 "To promote economic efficiency in the ... distribution of electricity" is an EA "purpose"
41 and an OEB Act "objective". Comprehensive system planning for overall economic
42 efficiency is something that an LDC must do to strive to meet that goal. The respective
43 purposes and objectives of the EA and the OEB Act also require LDCs "to provide

1 generators, retailers and consumers with non-discriminatory access to ... distribution
2 systems in Ontario”. Notably, Section 26(1) of the EA states that this latter objective is to
3 be provided by the LDC “in accordance with its licence”. Licences granted to all LDCs
4 are consistent in setting out two obligations with regard to connecting customers. First,
5 the licences state that LDCs have an obligation to connect a customer that “lies along” its
6 lines. This first licence condition is a restatement of section 28 of the EA. The second
7 licence condition is that an LDC must make an offer to connect customers within its
8 licensed service territory. Section 29 of the EA, which requires the LDC to sell electricity
9 to every person connected to its distribution system, complements these other sections in
10 that it requires the LDC to be ready at all times to connect customers and provide access
11 to the competitive commodity market.

12
13 In addition to these statutory and licence provisions, the DSC sets out definitively the
14 minimum conditions that an LDC must meet to fulfill the obligations of its licence. For
15 example, section 3.4.1 specifically states that distributors must “plan and build the
16 distribution system for reasonable forecast load growth”. Further confirmation is found in
17 Appendix B of the DSC, which requires LDCs to include the forecast of “customer
18 additions” in the economic evaluation model for expansion. Therefore, every LDC must
19 ensure that it has sufficient assets, whether wires or customer systems, available at the
20 appropriate time to provide service to customers. An LDC without such facilities at the
21 required time could be in breach of its obligations under these three sections of the EA
22 and the DSC, which provide the foundation for the obligation of LDCs to plan for future
23 growth and serve customers.

24
25 While the EA transformed the public sector, not-for-profit municipal electric utilities
26 (“MEU”) into commercial LDCs, it did not change these two obligations. From the
27 passage of the PCA 1906 to the introduction of the ECA in 1998, a municipality had the
28 right, under the PCA and PUA, to establish an MEU for part or all of its own
29 municipality (but beyond the municipal boundary only when provided by special statute).
30 Under the MFA, a municipality that did not purchase power from Ontario Hydro or its
31 predecessor could grant a franchise to a private utility, which could serve neighbouring
32 communities through additional franchise agreements (e.g., Cornwall Electric, Granite
33 Power). Pursuant to the PCA, Ontario Hydro served all portions of Ontario in which there
34 was no MEU or private utility. The resulting monopoly imposed on all utilities the
35 common law obligation to serve, which necessarily included the obligation plan.
36 Additionally, Ontario Hydro also had an obligation to plan for the MEUs embedded in its
37 low-voltage system.

38 39 **Public Utility Boundary Changes Prior to the ECA, 1998**

40
41 The PCA provided for a formalized, detailed arrangement for the transfer of assets
42 between Ontario Hydro and MEUs, in both directions. Municipalities were entitled to
43 purchase Ontario Hydro’s assets within their municipality in order to create or expand an

1 MEU. Conversely, Ontario Hydro had a statutory obligation to absorb a municipality's
2 MEU if it chose to go into the residual provider arrangements (e.g., Braeside in Renfrew
3 County, Courtwright in Lambton County). This ability to exchange assets was not,
4 however, inconsistent with the statutory and common law framework for discrete service
5 territories for planning growth and serving customers, nor did it interfere with Ontario
6 Hydro's ability to plan comprehensively for its "rural power district".

7
8 While the perception exists that Ontario Hydro was exposed and subject to significant
9 annexation by MEUs, this was not the case. Until the 1970s, most MEUs served only
10 traditionally defined cities, towns and villages, and thus already served to their full
11 boundary. The consolidation of a number of rural and urban lower-tier municipalities in
12 tandem with the creation of regional governments (e.g., York Region in place of York
13 County) in the 1970s created an environment for annexation, but only in 10 of the 49
14 county or northern district areas then in existence. Not all annexed, however. If the new
15 amalgamated municipality had a sizeable MEU or growing suburban character, it
16 generally had a business case to annex Ontario Hydro's assets (e.g. Markham, Vaughan,
17 etc.). If it had only a small MEU, the municipality tended to leave the rural system with
18 Ontario Hydro (e.g., Scugog Hydro in the old Village of Port Perry). The latter avoided
19 both the obligation to pay acquisition costs and the impact of rural operating costs on a
20 small MEU's rates. The result was that the MEU served only a portion of the newly-
21 expanded municipality.

22
23 To facilitate annexations, the PCA included statutory mechanisms not only for Ontario
24 Hydro's transfer of assets and territory to MEUs, but also provisions to ensure that
25 Ontario Hydro's customers were held harmless. The basis for the compensation of
26 Ontario Hydro in this public sector, non-commercial framework was to impose upon the
27 annexing MEU the obligation to pay for the assets and all costs that would be
28 underutilized or stranded as a result of the annexation. These annexation provisions
29 received their fullest exposition in the Bill 185 amendments to the PCA in 1994.
30 However, the amended PCA identified just 47 of the more than 800 municipalities in
31 Ontario as being eligible to annex Ontario Hydro's assets to their MEU. Prior to this right
32 ending in with the passage of the ECA in 1998, only 22 of the 47 municipalities, totaling
33 63,000 Ontario Hydro customers, had proceeded with annexations.

34 35 **Commercial Utility Boundary Changes Since the ECA, 1998**

36
37 In replacing the former statutory framework, the EA and OEB Act included a number of
38 features relevant to this interrogatory's issues of planning for growth and serving
39 customers. First, the new statutes took the MEUs and Networks out of the not-for-profit,
40 non-commercial public utility framework and put their replacement, LDCs, into a
41 commercial, for-profit utility framework. Second, the new statutes disentangled MEUs
42 from their municipalities and municipal legislation, such as the *Public Utilities Act*,
43 making them corporations under Ontario's *Business Corporations Act*. Third, the new

1 statutes did not continue the right of a municipality to establish a new MEU/LDC or to
2 expand an existing LDC to a municipal boundary. Fourth, the new statutes replaced the
3 previous public sector compensation scheme – no longer applicable because there is no
4 longer a statutory right of annexation – with the opportunity to merge, acquire or sell,
5 etc., without reference to any municipal or other boundaries (e.g., Veridian Connections,
6 Essex Powerlines). Fifth, while the service territory of LDCs is “non-exclusive”, the fact
7 remains that an LDC can operate only with a licence, and the Board has ensured that the
8 licences have distinct territories. All this evidence, coupled with the obligations imposed
9 upon the licensed LDC by the EA, the OEB Act, the DSC and the LDC’s licence, make it
10 clear that the licensed LDC continues to have an obligation to plan and serve customers
11 in its licensed territory and only in its licensed territory, regardless of municipal
12 boundaries, unless and until the licence area is amended.

13
14 These five features of the EA and OEB Act, and the obligation to plan and serve for the
15 area covered by the LDC’s licence, can be seen clearly when assessed against some of the
16 potential issues presented by this interrogatory if it is determined that “non-exclusive”
17 territory means that neighbouring or other LDCs can plan for the growth in the
18 incumbent’s service territory. This is a critical issue because all LDCs want growth, and
19 no LDC wants to lose either existing customers or new customer growth: LDCs are
20 already exposed to significant business challenges from the new performance-based
21 regulatory environment. While the rates of the former MEUs and Ontario Hydro were “at
22 cost”, regardless of the cost components or the cost of the annexations, an LDC cannot be
23 expected to be commercial under such circumstances. Indeed, all LDCs will be expected
24 to meet PBR improvements, but with a shrunken customer base or the loss of an area in
25 which customer growth would have occurred, the LDC will have a weakened ability to
26 cover its fixed costs and a deteriorating financial and risk profile.

27 28 **Obligation to Plan and Serve under Competition for Customers**

29
30 The potential for applications to the Board for service territory amendments to proliferate
31 is high if the Board were to find that the new legislation’s abandonment of reference to
32 municipal boundaries was unintended and that municipal boundaries are somehow still
33 relevant when the Board considers service territory amendment applications. The reason
34 is that Ontario has recently experienced unprecedented amalgamation of rural and urban
35 municipalities. This has occurred in the areas previously without regional government
36 (Savings and Restructuring Act, 1996) and the regional government areas have
37 experienced further amalgamations in Ottawa, Hamilton, Sudbury, Haldimand and
38 Norfolk (Better Local Government Act, 1999). While these amalgamations reduce the
39 number of Ontario municipalities to 445 from 815, the result is that there are now a larger
40 number of LDCs serving less than the full municipality where they are present. Further
41 municipal restructuring is also a possibility.

1 There are now 73 instances of two or more LDCs in one amalgamated municipality, up
2 from the 47 (in 1994). This is the case even though the number of LDCs was
3 consolidated to 95 from 306 MEUs. Kingston actually has three LDCs within its
4 municipal boundary – Kingston Electricity Distribution, Networks, and Eastern Ontario
5 Power (formerly Granite). Of the 95 LDCs, Networks estimates that 45 serve a full,
6 single municipality, 3 serve all the municipalities where they are present, 31 serve less
7 than the single municipality where they are present, and 16 do not serve all of the more
8 than one municipalities where they are present. This is a critical issue to Networks
9 because it has approximately 300,000 customers – 25% of its customer base – in
10 municipalities that also have another LDC.

11
12 Another problematic issue that would result from a finding that “non-exclusive” territory
13 means the incumbent LDC does not have the obligation to plan for growth and serve
14 customers is the sheer number of places where disputes over serving customers could
15 occur. While there are now 95 LDCs, there are in fact 202 distinct service territories. The
16 applicants and intervenors in this hearing demonstrate the case: by Networks’ count, Erie
17 Thames has 11 service territories, Veridian has 9, Essex has 4, and Westario has 14. If the
18 Board were to find that the legislation intended there to be competition between LDCs for
19 connections, the 202 boundaries could actually increase with new embedded service
20 territories, as has been requested by Essex Powerlines and Wirebury. For Networks,
21 which borders on 195 of the 202 service territories, this is a significant issue.

22
23 If the Board were to accept that the obligations to plan for growth and serve customers
24 are non-exclusive, the financial implications for both the applicant and incumbent
25 distributors would be significant. The incentive to consolidate through the MAADs
26 process under section 86 of the OEB Act would be diminished if the licence amendment
27 process were used to permit growth without acquisition transaction costs or loss of
28 control through mergers. In addition, if the Board were to revert to the public sector
29 compensation scheme that existed prior to the EA and OEB Act, it would in effect be
30 financially rewarding the applicant by permitting increased business value of the
31 applicant without commercial compensation to save harmless the incumbent LDC’s
32 customers. This issue affects all LDCs, municipal and private, not just Networks.

33
34 Please also see Networks' Prefiled Evidence, Appendix A, p. 4., lines 7 to 15.
35