

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S. O. 1998, c. 15 (Schedule B)

AND IN THE MATTER OF applications by Centre Wellington Hydro, Veridian Connections Inc., EnWin Powerlines Ltd., Erie Thames Powerlines Corp., Chatham-Kent Hydro Inc., Essex Powerlines Corp., Cooperative Hydro Embrun Inc. and Hydro One Networks Inc. pursuant to subsection 74(1) of the *Ontario Energy Board Act, 1998* to amend Schedule 1 of their Transitional Distribution Licences.

Submissions of Toronto Hydro-Electric System Limited with respect to the question of the Ontario Energy Board's jurisdiction to make an order which would have the effect of transferring a Distributor's existing customers to another distributor which has sought an amendment to expand its service territory

May 15, 2003

Introduction

1. At the April 30, 2003 Issues Conference in this proceeding, an issue arose with respect to the jurisdiction of the Ontario Energy Board (the "OEB") to make an order which would have the effect of transferring a Distributor's existing customers to another distributor which has sought an amendment to expand its service territory.
2. In Procedural Order No. 4 in this proceeding, the OEB gave the following direction:

"Hydro One Networks shall file with the Board a clear statement of the jurisdictional issue, including all relevant legislative references. Hydro One shall provide a copy of this statement to all parties to the Combined Distribution Service Area Amendment Proceeding. This material is to be filed and copied to all parties no later than May 8, 2003."
3. On May 8, 2003, Hydro One Networks Inc. ("Hydro One") circulated the following statement of the issue:

"Do the licence amendment provisions of the *Ontario Energy Board Act* give the Ontario Energy Board the jurisdiction to make an order which would have the effect of transferring a

Distributor's existing customers to another Distributor which has sought an amendment to expand its service territory, or does the Board have power only to consider licence amendments which would have the effect of transferring new customers?"

Parties wishing to participate in the argument relating to the jurisdictional issue were requested to file written submissions and the authorities upon which they intended to rely, with the OEB. Toronto Hydro-Electric System Limited ("TH Electric System") takes this opportunity to do so.

Toronto Hydro-Electric System Limited Submissions

4. TH Electric System submits that the licence amendment provisions of the *Ontario Energy Board Act 1998* (the "OEB Act") do not provide the OEB with jurisdiction to make an order that would have the effect of transferring a Distributor's existing customers to another Distributor that has sought an amendment to expand its service territory.
5. The basis for, and reasons in support of this position are described below.

The OEB's jurisdiction is restricted to those matters conveyed to it through the Board's enabling legislation.

6. TH Electric System submits that it is settled that the authority of an administrative tribunal is limited by its enabling legislation. In Re Hughes Boat Works Inc. and International Union, United Automobile, Aerospace, Agricultural and Implement Workers of America (UAW) Local 1620 et al. (1979), 26 O.R. (2d) 420 (Div. Ct.), the Ontario Divisional Court (Reid, J.) held that:

"It is accepted that tribunals are established to perform tasks frequently in a particular way but always within a limited frame of action. The limits are set by the legislative charter to which each tribunal owes its authority. Tribunals have no inherent powers; any they have must spring from legislation." (at p.425)

7. Given the critical importance of a Distributor's customer base to its revenue requirement and ability to collect that revenue requirement, such a fundamental power as the power to transfer existing customers from an incumbent distributor to a distributor applying for a service area amendment would have been expressly provided for in the legislation, particularly where the practical effect of such a transfer would be to extinguish property rights and commercial interests of the affected ("incumbent") Distributor, through the stranding of the incumbent Distributor's assets and the elimination of revenues generated for the incumbent Distributor from those customers. However, such authority is not found in the licence amendment provisions of the OEB Act, or in the OEB Act as a whole.

8. Not only is there no such express authority, but, as discussed below, the relevant provisions of the OEB Act that do address the transfer of assets either prohibit that transfer or contemplate an agreement between willing parties for the transfer of assets, that is then submitted to the OEB for its review and, if appropriate, its approval.

The OEB Act expressly provides that licence conditions shall not require disposition of assets.

9. Section 70 of the OEB Act permits the Board to prescribe conditions under which a person may engage in various activities, including the ownership and operation of a distribution system. However subsection 70 (13) limits the type of licence conditions the Board may impose. Specifically, this section prescribes that:

A licence under this Part shall not require a person to dispose of assets or to undertake a significant corporate reorganization.

10. Section 3 of TH Electric System's Transitional Distribution Licence No.ED-1999-0193, issued by the OEB on April 1, 1999, provides that "The Board, in the exercise of the powers conferred by Part V and subsection 129(1) of the *Act*, subject to the conditions of this Licence, licenses the Licensee to own or operate a distribution system in the service area described in Schedule 1 of this Licence." Schedule 1 contains the description of the TH Electric System service area. TH Electric System understands that this is a standard licence provision.

11. Any amendment of an existing distributor's service area will require an amendment to its own distributor licence and that of the other distributor(s) whose service area(s) will be affected by the first distributor's amendment. Similarly, a prospective distributor applying to establish a new service area will require a licence that sets out its own service area, and an amendment to the service area of at least one existing distributor. The amendment of service areas is therefore linked to distributor licences. The Board has no authority to impose a licence condition on an owner and operator of a distribution system that has the effect of requiring a disposition of its assets, regardless of whether the application before the OEB is for the amendment of an existing service area or the establishment of a new service area.

The OEB has no authority to transfer the assets of a Distributor that has been replaced by an interim licensee.

12. The OEB may issue an interim licence under section 59 of the OEB Act, authorizing a person to undertake any of the activities described in section 57 if the Board considers it necessary to do so to ensure the reliable supply of electricity to consumers.

13. Where the Board has determined that a distributor has failed to meet its obligations under section 29 of the *Electricity Act, 1998*, it may require the licensee, as a condition of an interim licence, to take possession and control of the business of the distributor; order the distributor to surrender possession and control of its business to the interim licensee; and without a hearing, amend or suspend the licence of a distributor.
14. The interim licensee may maintain and add to the property of the business and receive the income and revenue of the business, subject to such conditions as the Board may determine, and may dispose of such assets as are ordinarily disposed of in the normal course of carrying on the business of a distributor, but the OEB may not order the transfer of the distributor's assets to the interim licensee. Subsection 59(10) of the OEB Act provides that,

“Despite subsection (2) or (3), and subject to subsection (4) a distributor to whom an order is issued under clause (2) (b) retains ownership of any assets of the business that the distributor owned before the order was issued, subject to any encumbrances.”

Accordingly, even where another entity, and conceivably another Distributor, is operating an incumbent Distributor's system, the OEB has no authority to transfer the incumbent Distributor's assets.

The OEB Act has provided for the transfer of existing assets through the MAADs process.

15. TH Electric System submits that the Legislature has already considered the circumstances in which a distributor's existing assets could be transferred to another distributor – that is in the context of a sale, lease or other disposition of a transmission or distribution system as an entirety or substantially as an entirety, or any part of a transmission or distribution system that is necessary in serving the public, as provided for in section 86 of the OEB

Act. While the section does not speak explicitly to the transfer of customers, this is the necessary implication of any transfer of a distribution system. The sale, lease or other disposition will come about through an agreement negotiated between the parties, and there is no provision for the OEB to initiate such a process.

A Distributor's customers constitute distribution assets.

16. The central purpose of a distribution system is to serve customers. If no customers exist there is no need for a distributor. The only means through which distribution systems generate revenue is through the conveyance of electricity to actual customers. Without rate paying customers, the physical assets that comprise a distribution system are essentially worthless.
17. Given the pivotal role customers play as the prerequisite and rationale for providing distribution services, TH Electric System submits that customers comprise an integral component of a Distributor's assets, and must be considered as falling within any reasonable interpretation of the term "assets".
18. TH Electric System submits that the interpretation of "assets" referred to in section 70(13) as including a Distributor's customers is supported by central rate making principles embodied in section 78 of the OEB Act, and implemented through the OEB's Electricity Distribution Rate Handbook (the "Rate Handbook").
19. Subsection 78(2) of the OEB Act provides that, "No distributor shall charge for the distribution of electricity or for meeting its obligations under section 29 of the Electricity Act, 1998 except in accordance with an order of the Board, which is not bound by the

terms of any contract.” Subsection 78(3) in turn provides that, “The Board may make orders approving or fixing just and reasonable rates for the transmitting or distributing of electricity and for the retailing of electricity in order to meet a distributor's obligations under section 29 of the *Electricity Act, 1998*.” While an application for a rate order under section 78 may now be made only with the written approval of the Minister of Energy pursuant to section 79.6 of the OEB Act, the power to make a rate order still lies with the OEB.

20. The Rate Handbook defines distribution activities and assets as follows:

“Activities that enable the conveyance of electricity for distribution purposes will be considered to be distribution activities. Consequently, assets associated with activities that enable the conveyance of electricity for distribution purposes will be considered to be distribution assets.” (Rate Handbook, Appendix D, Page 2, Section 2.1).

21. The Rate Handbook goes on to identify several activities that are considered to be distribution activities including, among others, meter reading service, billing and collection, energy education and customer care, etc. (Rate Handbook, Appendix D, page 3). Since customers are necessarily associated with all these activities it is submitted the Board should interpret distribution assets in section 70(13) as encompassing both the physical infrastructure and equipment needed to convey electricity to the customer as well as the customers themselves.

22. Similarly, the Rate Handbook defines the electricity distribution utility rate base as “the year-end net fixed assets (distribution ‘wires only’) plus a working capital allowance.” (Rate Handbook, section 3.4.1.1) The rate base is fundamental to the calculation of a distributor’s Market Adjusted Revenue Requirement, which in turn is critical to the

establishment of the distributor's rates. In addition, while the OEB's service quality standards address the level of service provided through a distributor's physical assets, the standards are all customer-related. For example, the OEB's SAIDI (total customer-hours of interruptions ÷ total # of customers served), SAIFI (total customer interruptions ÷ total # of customers served) and CAIDI (total customer-hours of interruptions ÷ total # of customer interruptions) indices are all intrinsically linked to the distributor's customers. Without customers, the distributor's rates and service quality are as irrelevant as its physical assets.

23. Accordingly, because a distributor's customers are inextricably bound to its physical infrastructure assets, TH Electric System submits the Board has no jurisdiction to transfer existing customers of a distributor, for the reasons set out in the preceding portions of this submission, and particularly since the mandatory disposition of distribution assets as a licence condition is expressly prohibited by law.
24. Moreover, TH Electric System submits that any provisions of the OEB Act that speak to the transfer of assets do not grant the OEB the authority to transfer existing customers of a distributor at the request of a single party and in the absence of an agreement between the incumbent and prospective distributor.

The transfer of existing Local Distribution Company ("LDC") customers in the context of a service area amendment application would also be contrary to the OEB's guiding objectives since the consequences would be the further destabilization of the Ontario electricity distribution sector.

25. In addition to the foregoing, the Board must be mindful of the guiding objectives contained in section 1 of the OEB Act. TH Electric System submits that the transfer of

existing customers as part of a service area amendment would be beyond the jurisdiction of the Board since such transfers would be contrary to the following section 1 objectives:

- to protect the interests of consumers with respect to prices and the reliability and quality of service (Objective 3);
- to promote economic efficiency in the distribution of electricity (Objective 4);and
- to facilitate the maintenance of a financially viable electricity industry (Objective 5).

26. Customer transfers may result in the transferor distributor being left with stranded infrastructure and equipment through the loss of existing customers. Allocation of stranded costs to the remaining customers of the transferor distribution system will result in higher distribution rates for the incumbent distributor's remaining customers than if the existing customers remained with the incumbent distributor. It is submitted that this scenario would violate the price protection and economic efficiencies focus which the Board has been directed to consider.

27. Furthermore, the recent distribution rate freeze imposed by the province through the *Electricity Pricing, Conservation and Supply Act, 2002* ("Bill 210") has created new financial pressures on LDCs until 2006. The Board will be aware that credit rating agencies and other industry stakeholders have expressed concern about the regulatory environment for Ontario's electricity sector, and Standard & Poor's Ratings Services recently placed various Ontario Distributors or their parent companies on "CreditWatch with negative implications". TH Electric System suggests that Bill 210 legislative changes, regulatory and political risks surrounding the freeze on LDC rates of return, and the uncertainty relating to the recovery of various regulatory assets and transition costs by Distributors are important factors which underline these concerns.

28. In TH Electric System's submission, the LDC sector would be further destabilized if the Board were to approve the transfer of existing customers as a result of licence amendment proceedings regarding service area amendment. Both historically and currently, LDCs make investments in their business on the basis of future revenue flows from customers. Were the Board to introduce another element of uncertainty and possible financial exposure for LDCs, through the prospect of the loss of existing customers, this would add further doubt concerning the long-term financial integrity of LDCs. Such a result would be contrary to the guiding objective to maintain a financially viable electricity industry.

Conclusion

29. In light of the foregoing, TH Electric System submits that the licence amendment provisions of the OEB Act do not provide the OEB with jurisdiction to make an order that would have the effect of transferring a Distributor's existing customers to another Distributor that has sought an amendment to expand its service territory.

All Of Which Is Respectfully Submitted:

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