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February 9, 2004

Paul B. Pudge, Assistant Board Secretary
Ontario Energy Board
26th Floor, 2300 Yonge Street
Toronto, Ontario M4P 1E4

via facsimile 416.440.7656 – Original to follow by courier

Dear Mr. Pudge:

**RE: Toronto Hydro Comments Regarding Staff Report on DSM and DR
OEB File No. RP-2003-0144**

Please find enclosed nine (9) copies of Toronto Hydro's comments on the Staff Report to the Board in this matter. Also enclosed on diskette, is an electronic version in PDF format.

Kindly direct all questions or comments to the undersigned.

Yours truly,

"R. Zebrowski"

R. Zebrowski, Vice-President
Regulatory Services

Toronto Hydro
Comments on Staff Report to the Board on
Demand-Side Management and Demand Response

Introduction

1. Toronto Hydro has participated actively in the RP-2003-0144 proceeding, and appreciates the opportunity to provide comments on the Staff Report to the Board on Demand-Side Management and Demand Response. Toronto Hydro represents both Toronto Hydro-Electric System Limited (TH Electric System, the distribution utility) and Toronto Hydro Energy Service Inc (THESI, the energy services and electricity retailing company).
2. Toronto Hydro was a member of the Advisory Group formed by the Board. During the course of this proceeding and in the context of the Advisory Group discussions, Toronto Hydro made its general views concerning DSM and DR known verbally and in writing. Toronto Hydro continues to rely on its previous submissions.
3. Toronto Hydro will confine its remarks here to the proposals set out in the Staff Report and to alternative approaches that it believes would be preferable. Toronto Hydro will not use this occasion to respond to all of the concepts that were put forward by various parties in the Advisory Group Report.

4. For clarity, and in keeping with the format of the Staff Report, the comments that follow are divided into separate sections that address DSM and DR individually. However, Toronto Hydro believes there are many areas where DSM and DR overlap and where it would be efficient for them to be undertaken jointly.

Toronto Hydro Position Summary

5. The two factors that will most contribute to the early achievement of DSM and DR are the ending of subsidized electricity prices and a stabilized policy environment.

6. The main focus now should be on removing existing barriers to effective DSM and DR, and delivering programs using resources that are already in place or that can be deployed quickly.

7. Utilities have a vital role to play in achieving early successes in DSM and DR. Toronto Hydro continues to support a role for utilities that would address DSM and DR barriers related to rate structures and metering, and proceed to focus on the delivery of programs to customer classes where the largest and fastest gains can be made.

8. The approaches to achieving DSM and DR will need to be tailored to the differing customer segments to which they will apply. In the residential and small commercial classes, a centralized mass-market approach could be appropriate to ensure consistency, wide program availability, and cost effectiveness. As customer size and sophistication increase, a more customized approach will be needed.

9. Utilities can exploit their knowledge of local markets and relationships with customers, especially in the business customer classes, to make early headway in DSM and DR. In many cases, this could be achieved through cooperation with existing energy service companies.
10. Toronto Hydro acknowledges that a centralized role for certain planning and design functions is needed, particularly in the mass-market areas. However, the centralized role should be confined to that which is necessary to achieve consistent program design, scale economies, and efficient administration. The primary responsibility for program delivery should rest with utilities.
11. Regardless of who designs and delivers programs, utilities should not be adversely affected financially by the achievement of DSM and DR. A variety of approaches are available to remedy the problem of revenue erosion for utilities, and the OEB should ensure that this problem is effectively addressed.
12. Toronto Hydro believes that significant levels of DSM and DR can most quickly and efficiently be achieved through a system of transparent and meaningful incentives for providers, rather than through a new bureaucratically driven process.

Toronto Hydro Comments on the Staff Report

Demand Side Management

13. Toronto Hydro acknowledges that there is a need for central co-ordination, policy setting, and other functions. However, it has concerns that a Central Agency as described in the Staff Report would take a considerable amount of time, money, and human resources to construct, and that achievement of important DSM and DR targets would be postponed as a result.

14. Despite assurances in the Staff Report that a Central Agency would become redundant as the 'conservation culture' flourished, Toronto Hydro is not confident that the agency could avoid becoming entrenched with strong incentives for self-perpetuation. Toronto Hydro suggests that if such an agency is established, its performance be evaluated after 3 years and at regular intervals thereafter to determine whether it is effectively meeting any ongoing needs. The agency's ongoing existence should be subject to acceptable findings in such reviews.

15. Furthermore, under the funding mechanism proposed in the Staff Report, the Central Agency would be funded by an unavoidable electricity consumption tax (i.e., the system benefit charge, or SBC). Toronto Hydro takes the view that strong safeguards and cost-effectiveness tests would be needed indefinitely to ensure that the SBC did not become a liberal source of funding for undisciplined expenditures. Toronto Hydro suggests that it may be

reasonable to devote the 2005 MBRR funds to the agency with the proviso that the need and form of any ongoing funding, as well as the effectiveness of the 'seed' funding provided thereby be evaluated at the first review of the agency (i.e., after 3 years).

16. These concerns are mentioned at Section 3.1.2 of the Staff Report. In very general terms, the Staff Report states "Transparent reporting of results and periodic review of effectiveness would ensure that the agency was accountable and did not outlive its usefulness."

17. It is unclear whether the Board would ultimately acquire the responsibility to regulate such a central agency, or failing that, in what manner if at all it would be regulated.

18. Taken altogether, Toronto Hydro does not support the formation of a new bureaucracy with a guaranteed involuntary revenue stream, which would itself require regulation that could be costly and/or ineffective.

19. The Staff Report goes on to express the view that utilities face inherently contradictory incentives with respect to load building versus conservation.

20. A number of remedies exist to address the problem of DSM-related revenue erosion for utilities. While Toronto Hydro believes that Lost Revenue Adjustment Mechanisms (LRAMs) are too unwieldy to implement for electric utilities, other options are available. Toronto Hydro would prefer the use of annual updates of volumetric forecasts, which would be used to reset rates to recover the existing approved revenue requirements. Alternatively, a Revenue Cap per Customer form of PBR could be adopted. Therefore, Toronto Hydro

does not view the objection concerning utility conflicts between conservation and load building as being irresolvable.

21. The Staff Report also expresses concerns that utilities not be uncompetitively advantaged in the delivery of DSM and DR.

22. Toronto Hydro has no wish to obtain unfair competitive advantages for its distribution utility or its retail operation. THESI will continue to compete in contestable markets according to its business plan and new opportunities that emerge. TH Electric System is essentially a non-competitive natural monopoly distributor.

23. The Staff Report further states at page 14 “An alternative to the Central Agency model is the use of utilities to deliver DSM and DR activities.” In the context, this implies that under the Central Agency model utilities should be involved with DSM and DR only on their own distribution systems.

24. However, Toronto Hydro and other utilities are uniquely positioned to encourage and enable increased conservation practices among their customers through ‘infrastructure’ investments and activities, principally in the areas of metering, rates, and customer contact. Utilities have ongoing, vital relationships with their customers, and Toronto Hydro believes that customer acceptance and take-up of DSM and DR programs will be greater if they are offered through utility channels.

25. Additionally, there may be opportunities for utilities to realize significant energy conservation on their own distribution systems. In principle, Toronto Hydro supports the Staff Report recommendation that utilities be provided with incentives to cost-effectively decrease losses on their systems.

26. Therefore, Toronto Hydro believes that utilities should play a prominent role in DSM/DR, with respect to program delivery, distribution system equipment optimization, metering, rates, and customer communications.

Demand Response

27. The greatest economic and environmental benefits will be obtained from effective demand response. Toronto Hydro also believes that in the short term, the greatest demand response can be obtained from large, sophisticated electricity users, assisted by improvements to price transparency and the system of future price discovery.

28. Toronto Hydro supports efforts by the IMO and others that are underway to encourage effective demand response, and generally endorses the discussion of DR in the Staff Report. Toronto Hydro supports 'economic' DR programs (i.e., those involving side payments to reduce demand) during periods of supply shortage, and acknowledges that they could produce net benefits in the short term through stimulating the development of infrastructure and readiness necessary to achieve effective DR.

29. Small loads in isolation cannot effectively participate in DR. Load aggregation is needed to permit the participation of smaller customers. Therefore, Toronto Hydro supports the concept of utilities and other energy market participants providing load aggregation services when those services are economically justified.

30. Toronto Hydro strongly supports movements toward cost-effective time-differentiated metering for customers currently without this. In order to be meaningful, time-differentiated metering must be combined with time-differentiated commodity rates. Toronto Hydro urges the Board to fully consider time-differentiated commodity rates in its current investigation of Standard Supply pricing strategies.