

Presentation by: Halton Hills Hydro Inc.
“Review of Further Efficiencies in the Electricity Distribution Sector”

Presented by: Bryan Boyce – Chair and Dan Guatto – President

1 Background:

2

3 Halton Hills Hydro Inc. (Halton Hills Hydro) is a utility on the western edge of the
4 GTA of approximately 18,500 customers with expected increases of an additional
5 1000 customers in 2004/2005. The customer mix is weighted to the residential
6 class and the community has a high proportion of its land area used in the
7 practice of agriculture. The utility serves a number of large customers and
8 economic development patterns along the transportation corridors indicate the
9 number of customers in this class will grow.

10

11 The utility operates to the municipal boundary of Halton Hills, and has a staff of
12 approximately 40 providing all basic and regulated utility services in a single unit.
13 The company prides itself on low cost and effective service with particular
14 reference to the residential class of customers.

15

16 The Board of Directors of this utility is engaged in the management of the utility.
17 The Board of Directors is dedicated to the pursuit of continuous improvement
18 particularly in worker and public safety, system reliability, customer care and
19 service management, and compliance in the regulatory forum. In addition, they
20 are well attuned to the community and the provision of value to the shareholder –
21 the Town of Halton Hills.

22

23 Purpose of Appearance:

24

25 Halton Hills Hydro is and operates in all ways as an effective and efficient utility
26 company. Residential rates are the lowest of the surrounding utility group.
27 Success in streamlined business planning, effective management of utility
28 resources from inventory to computer support, and budgets that are developed

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1 using previous fiscal year actual results to provide targets for continuous
2 improvement have proven to result in our ability to maintain this cost efficiency.

3
4 Halton Hills Hydro Inc. adapts to change well, and its staff is an important
5 resource to help achieve that capability. It may be important to note their ability to
6 work as a team to manage new regulatory and legislative initiatives and to
7 establish appropriate responses within efficient time frames to adapt our
8 operations as required. We don't rely on specialists on a day-to-day basis
9 although and we make limited use of consulting services.

10
11 The purpose of this presentation is to identify some of the concerns Halton Hills
12 Hydro have with the possible direction of the OEB as outlined in the discussion
13 paper. Board Staff's paper "Review of Further Efficiencies in the Electricity
14 Distribution Sector", February 10, 2004 almost suggests there is a degree of
15 frustration that further consolidation did not occur as a result of the transfer tax
16 exemption offered in 2003. A number of individuals have expressed the need for
17 change to continue, and learned papers have been written about the benefits of
18 consolidation or rationalization. No specific analysis from which to establish a
19 true test of the effectiveness of consolidating utilities in Ontario has been
20 provided. In fact, simply being small has been the criteria more often used for
21 rationalization without consideration of other parameters - one in particular being
22 the satisfaction of the customers served by the smaller utilities.

23
24 Also, the need for rationalization has been linked to administrative and regulatory
25 "drag" in terms of time delays and the negative influence that has on the ongoing
26 evolution of the electricity sector. From my perspective, this is an important
27 problem, but it may be the least of the problems that must be dealt with
28 effectively by government and the regulator. The need to meet supply and

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1 demand side management initiatives is more serious. Despite the criticisms of
2 the sector, distribution utilities provide necessary services that are for the most
3 part supported by local customers. Distribution utilities are able to adapt and to
4 undertake new challenges, as the electricity market requires. Regulatory
5 workload should not be the reason to eliminate efficiently operating utilities by
6 statute.

7

8 I was not surprised by the apparent lack of initiative to take advantage of the
9 transfer tax exemption. Simple business principles suggest that in an uncertain
10 political climate the investor will avoid undue exposure to risk. In addition,
11 municipal shareholders didn't want to react. Nor do I expect that there is a
12 political will generally available at the municipal level to engage in further activity
13 unless there is an absolute certainty that the business case is valid. If the utility
14 is profitable, and the consumers enjoy the services they have come to expect,
15 then new changes initiated by municipal owners are not likely to be received
16 favourably by the voting public.

17

18 It is important to test our efficiency collectively to ensure customers of electricity
19 products are getting the best for their investment. As I indicated earlier, Halton
20 Hills Hydro's Board of Directors does this as part of our normal operating
21 practice. It is important that the OEB not ignore the corporate governance role
22 played by the Directors.

23

24 So with this preamble to try to set context, I intend to move through the elements
25 of the Board's consultation paper and provide commentary.

26

27 Types of Efficiency Factors

28

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1 Operational Efficiency

2

3 The comments provided in the consultation paper for the most part are
4 appropriate for the ongoing evolution of the distribution sector. In reviewing the
5 context in this section, I took note of the apparent need to lecture utility operators
6 on the principles discussed with respect to customer service. In the middle of the
7 page (page 8) there is the following statement:

8

9 “...It is therefore desirable to develop mechanisms that encourage distributors to
10 strive to be responsive to customer perceptions of the trade-off between price
11 and standards of service.” (Page 8, “Review of Further Efficiencies in the
12 Electricity Distribution Sector”, February 10, 2004)

13

14 Later the paper suggests developing a “variety of price-service offerings” for the
15 distribution sector.

16

17 I have had the privilege of working in a very large utility and the now enjoy the
18 added privilege of working at a smaller distribution utility level. Unlike the large
19 utility, when I walk through the doors of the LDC there are people from the
20 community at the counter, or in the lobby one might see a group of development
21 engineers. They are a constant reminder that the opportunity to provide solutions
22 to customers’ needs is available and the opportunities are not limited to one or
23 two specific types. In truth, there is a higher degree of adaptability in the
24 distribution utility than could be achieved with the larger entity. This is evidenced
25 by the adaptations that have been made at Halton Hills Hydro to accommodate
26 market opening, deal with competitive pressures, and comply with regulatory
27 initiatives.

28

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1 Efforts to identify and to accommodate solutions that fit customers are being
2 delivered daily. Utility managers recognize that the ability to choose is a priority
3 for the customer. The utility should have the ability to offer choices to the
4 customer, and to be able to compete with other service providers of those
5 choices on an equal footing. Limitations imposed by regulation or uncertainty in
6 the delivery of provincial energy policy do not support utility efforts to adapt
7 prices and services as required to meet customer needs. Flexible regulatory
8 oversight should also be part of the package that delivers the options to provide
9 customers with meaningful choices between price and service level.

10
11 **Controllable Structural Efficiency**

12
13 Individual utilities are similar to all businesses handling a similar commodity or
14 stable of choices. Despite the basic or core similarities, each do unique things to
15 fit with their franchise area, their policy and business plan, or their community
16 and customer mix. Halton Hills Hydro supports a rural population and supports
17 two small towns separated by open land. Delivery of its services has
18 necessitated the evolution of a structural pattern supporting less use of
19 contractual services and more reliance on in-house services. Economies of scale
20 considerations are always a matter for consideration by management; however,
21 the Board of Directors expects that cost targets and efficiencies will be met using
22 any appropriate means at hand by the management team. Further, the Board of
23 Directors is both willing and able to impose strategies to affect the delivery of
24 expected financial results.

25
26 As Chair of that Board, I am concerned that the imposition of standards to push
27 or to pull us towards a certain business approach unnecessarily will deliver the
28 wrong message to the ratepayer and shareholder about efficiency, and increase

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1 further confusion among the consumers in each rate class. If efficiency in the
2 operation is evident and ongoing business operations suggest the efficiency will
3 continue, there should be sufficient regulatory flexibility to enable the operation to
4 continue. The OEB should deal with the inefficient elements through rate
5 applications or other normal regulatory interventions, but should not impose new
6 regulatory approaches to attempt to force economies of scale in situations not
7 demanding such consideration.

8

9 Uncontrollable Structural Efficiency

10

11 Uncontrollable structural efficiency is one of the characteristics of electricity
12 distribution that requires continuous adaptation by the utility to manage. This
13 creates a significant difficulty when attempting to impose efficiency through
14 legislation or regulation. More likely the solutions to problems created by
15 uncontrollable factors are to be found by the management of the utility. The utility
16 must adapt to these characteristics. There is a further requirement to ensure the
17 utility remains in compliance with regulatory protocols but once assured of this,
18 there should be regulatory flexibility to enable these solutions to work.

19

20 PBR is designed to help accommodate such uncontrollable structural changes.
21 The Board Staff paper recognizes this value of PBR and perceives
22 accommodation for such situations can be obtained. (Page 11, “Review of
23 Further Efficiencies in the Distribution Sector”, February 10, 2004).
24 Uncontrollable structural change can be mitigated by becoming informed and
25 knowledgeable about the characteristics of the distribution utility sector in
26 Ontario, and avoid imposing inappropriate external solutions to homegrown
27 problems. The answers to the problems of dealing with non-controllable

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1 structural efficiencies are likely to remain for the most part unique to the utility
2 and to its relationship with its regulator.

3
4 For example, within the municipal boundary of Halton Hills, Halton Hills Hydro
5 knows its business area has certain characteristics, certain expectations of
6 growth, and customer needs. Decisions made at the provincial and regional
7 government level are uncontrollable and may affect operations or need
8 adaptation to accommodate. However, the first level of reaction to these policy
9 changes is at the Board of Directors level, and that may require intervention at
10 the regional level, discussion among similarly affected utilities to determine a
11 pattern of response within the unique utility concerns. At some point the
12 regulator may or will be advised to ensure accommodation is a consideration.

13
14 To digress a bit, uncontrollable structural change has occurred at what appears
15 sometimes to be the whim of legislators relying on extra-provincial input simply
16 because not enough information is apparently available about the Ontario
17 market. Because things don't run smoothly quickly is not a function of doing
18 things wrong, it is more a function of the acknowledged complexity of supplying,
19 transmitting and delivering electricity. Low levels of patience among decision
20 makers to endure the challenges created by this complexity make the capability
21 of the electrical energy industry to be successful in as short a time period as
22 possible suspect. Inserting solutions from other jurisdictions does not create the
23 panacea. We need to become more introspective and make our own decisions.

24
25 Consumer Benefits: Economic, Service and Other Benefits

26
27 “...policies and measures that further efficiency of the distribution sector by
28 increasing customer value, rather than just reducing distributor costs, may be

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1 preferred.” (Page 12, “Review of Further Efficiencies in the Distribution Sector”,
2 February 10, 2004)

3
4 The market opened in May 2002. The market effectively closed in November
5 2002. Market or electricity industry changes have been ongoing since that time.
6 Customers are facing brown outs, black outs and fear that their costs will see no
7 ultimate stability. The uncertainty continues today.

8
9 There has been one constant throughout this period of uncertainty at Halton Hills Hydro.
10 The customer comes first, can walk through the front door and get answers albeit at times
11 to the best of our ability given the uncertainty. My position as Chair provides the
12 privilege of periodically meeting with the Mayor and councilors and interest groups about
13 the electricity industry. Assurances that the customer is being treated as well as possible
14 and as fairly as possible and that the value of the services to the customer is a priority are
15 not given by me to lighten the political load, but are the intention and the norm.

16
17 Notwithstanding the above, it is important to me that the business plan is a
18 balanced solution to the corporate direction, and the delivery of customer care
19 initiatives is delivered as a balanced component of distributor costs. One
20 significant factor is making sure the customer is well informed about the make up
21 of the bill, and the variety of charges identified not specifically attributable to the
22 distribution of their electricity to their home or office.

23
24 **Barriers and Incentives to Enhancing Efficiency**

25
26 The nature of distribution utilities has for the large part changed. Some entities
27 have yet to accommodate fully to that change. Some participants in the
28 distribution industry do not believe all utilities are capable of accommodating the

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1 new rules of engagement that have been established. I acknowledge that all of
2 the participants must ultimately become capable or face loss of credibility and
3 status.

4
5 However, this is not to say there should be a legislated solution. The decision to
6 change utilities to corporations under the OBCA is one valuable and necessary
7 solution to the delivery of better efficiency and services to the consumer. Neither
8 non-economic objectives nor absence of discipline should survive a properly
9 constituted Board of Directors with the mandate to deliver shareholder and
10 customer value.

11
12 The importance of the regulator delivering appropriate rules for operating
13 efficiently within the market is essential as well. A significant barrier to enhancing
14 efficiency will be a situation in which an effective utility is biased by a regulatory
15 attitude that small is wrong. In this context, the barrier raised can only be
16 removed by establishing appropriate measurement tools to enable meaningful
17 assessments of efficiency.

18
19

20 Experience Elsewhere

21
22 I wanted to note for the record that research into experiences in other
23 jurisdictions is pertinent to any activity. The danger in applying the research
24 results directly is clearly articulated in standard clichés associated with making
25 sure we are dealing with the same fruits before making adjustments. It is difficult
26 to assess how similar the Ontario situation is to the jurisdictions mentioned in the
27 Board Staff’s paper. The notable standard is that each has a government
28 interested in making the electricity sector work better - as do we.

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2 Policy Objectives and Evaluation Criteria

3

4 The OEB has a broad mandate to assist the electricity industry to become
5 successful. The individual components of this mandate are provided on page 18
6 of the “Review of Further Efficiencies in the Distribution Sector”, February 10,
7 2004. Ministry of Energy policy changes and directions to achieve quick results
8 result in significant pressure to move forward, perhaps without adequate time to
9 assess an appropriate approach. Overlaying the characteristics of another
10 jurisdiction onto this system in order to move more quickly to a potential solution
11 does not necessarily resolve the ongoing energy issues in the Province. In fact, it
12 is more likely to force another review.

13

14 With constant information flowing to it from the utilities, and formal rate
15 applications the OEB has the capability of assimilating a significant quantity of
16 data to support conclusions it may reach with respect to efficiency. The OEB is in
17 a position to cause research to be undertaken and to supply information to the
18 utilities on expected operational standards, to actually indicate the level of
19 efficiency associated with the utility’s operation.

20

21 It is important that the OEB have solid and appropriate information sources
22 concerning electric distribution utilities. Advisors should be knowledgeable about
23 the utilities and the regulatory environment. Electricity distributors are not the
24 same as gas utilities, nor do their operational characteristics make a direct
25 comparison easily achievable. The amount of time associated with decision-
26 making processes such as this one is limited. The effort to mold the components
27 of information provided through this review into a meaningful conclusion may be
28 adversely affected by bias towards a certain criteria (e.g., size) that is perceived

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1 to affect regulatory efficiency. The OEB must be wary of reacting to reports and
2 data that support no conclusions with regard to rationalization to achieve
3 efficiency.

4

5 Options to Consider and Further Issues for Discussion

6

7 Further Consolidation

8

9 The operating premise of this review is the need for further consolidations.
10 Information associated with rate applications and other reports to the OEB may
11 also provide an indication of that being the case. Reality suggests that such
12 consolidation may happen because a willing seller and a willing buyer enter the
13 same room together.

14

15 However, without that data and observing this situation from my position as Chair
16 of Halton Hills Hydro, I see no requirements to alter my utility operations. On
17 page 20 of the “Review of Further Efficiencies in the Distribution Sector”,
18 February 10, 2004, Board staff identify that 42 distributors may not meet a
19 minimum efficiency scale of customers. Generic policies and measures to
20 remove barriers to deal with improving efficiencies in these 42 utilities are not or
21 may not be in the best interests of the utilities in question. Some of these utilities
22 may provide meaningful services to consumers that could be lost. Individual
23 assessments may need to be completed prior to applying a policy direction to the
24 utility under scrutiny.

25

26 Incentives

27

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1 Incentive regulation has value if there are consistent standards to enable
2 measurement of efficiency. Whether the PBR program is effective for Ontario
3 utilities has not been seriously tested as yet because of anomalies created by
4 government and legislative change. Creating a meaningful analysis of the impact
5 of PBR on the public interest may not be conclusive at this time.

6
7 Consumers need to be allowed to stabilize their patterns of use by using
8 transparent and consistent pricing signals for a period of time. Utilities need to
9 begin an orientation to demand side management programs.

10

11 Load Serving Entities

12

13 There are difficulties for LDC's to transition to a Load Serving Entity that have
14 been outlined in the Board Staff's paper on page 22, the "Review of Further
15 Efficiencies in the Distribution Sector", February 10, 2004. The introduction of this
16 entity increases the level of uncertainty and complexity into the electricity supply,
17 transmission and distribution package to consumers. In particular, it raises the
18 possible specter of adding another line on the bill, one that might be as easy to
19 explain as "line losses". This option should not receive arbitrary support prior to
20 further detailed consideration in a specific forum. The significant added risk that
21 an LSE creates for a utility operation needs to be fully explored prior to making a
22 commitment. The possibility exists that the Load Serving Entity is not something
23 that increases efficiency for LDC's or the distribution sector but could in fact
24 detract from efficiency at the LDC level while adding nothing in return for
25 consumers.

26

27 Distribution System Planning

28

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1 With respect to the arguments associated with consolidation to support broader
2 more effective system planning approaches, the arguments are theoretical only.
3 Engineers like to achieve such simplicity in project management but the nature of
4 system planning does not preclude a group of utilities from hiring one consulting
5 group to produce the same results without consolidation. Nor does it preclude
6 engineering staff from each utility working as a team to accomplish this task. No
7 significant cost differences may result, however, integrated system planning will
8 happen no matter what structural form utilities may take. This is not an argument
9 for consolidation, however it is an efficiency issue if the utilities in the group
10 become intransigent with each other.

11

12 Technical Innovation

13

14 The point of this discussion in the “Review of Further Efficiencies in the
15 Distribution Sector”, February 10, 2004 on page 24 is elusive. A utility is of
16 necessity a state of the art technological entity. Technology does accelerate the
17 capability of the utility to be efficient in some ways and possibly in many ways. A
18 well-trained and technologically supported staff is more efficient.

19

20 Costs incurred for upgrades to metering systems and system monitoring
21 programs to enable these technological efficiencies to be effective in terms of
22 system reliability and customer responsiveness may minimize the ultimate cost
23 savings. It is not anticipated that this on its own is a reason to support increased
24 rationalization.

25

26 Concluding Remarks

27

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1 Halton Hills Hydro is a corporation established as a result of the *Energy*
2 *Competition Act, 1998*. It is a well run efficient local electric distribution company.
3 The Board of Directors, the staff and the shareholder have a specific interest in
4 continuous quality improvement and in providing the right services at the right
5 cost to our customers. Unfortunately, the business of electricity is not insular and
6 the impact of external operations by others, and the impact of policy makers and
7 regulators create the need to accommodate continual change as part of the
8 normal operating practice. To the extent to which we can control these changes
9 from creating adverse impact on the utility’s electricity system and the consumer
10 of the commodity and its associated services, Halton Hills Hydro will do so.

11

12 The challenge to accommodate these impacts is made the more difficult when we spend
13 time worrying that someone else is going to decide we are too small to work efficiently. I
14 suggest we need to channel our energies toward determining what can be done by the
15 utilities to help deliver necessary messages about energy efficiency, and load
16 management. Those utilities have been in the forefront of the energy industry in Ontario
17 meeting the customer face-to-face, and dealing with their problems. Distribution utilities
18 are part of the Ontario electricity landscape. Each of these utilities has a role to play and
19 no matter what size, effectively managed utilities are allies in the delivery of provincial
20 and regulatory policy.

21

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