

Written Presentation

To the

Ontario Energy Board Hearings RP- 2004-0020

on

Consultation on Efficiencies in the LDC Sector

By

North Bay Hydro Distribution Limited

Presented by: Ron Ross, General Manager

February 2004

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Introduction

The Ontario Energy Board (OEB) announced recently that they would be holding consultation on efficiencies in the LDC Sector. All participants had to declare by noon on Thursday, February 5, 2004 whether they planned to make a written and/or oral presentation to the OEB during the week of February 16th. North Bay Hydro Distribution Limited (NBHDL) registered to submit a written presentation by February 16th and an oral presentation on February 17th.

History

NBHDL is owned by the City of North Bay and serves a total of 23,000 customers over an area of 350 square kilometers. In July 2000 a Board of Directors was appointed by the city to replace the former commission and to administer the affairs of NBHDL. The objective was to operate the company as a for-profit private corporation that was responsible to the city through a holding company (Holdco). Shortly after taking control of the company, the board made a number of strategic decisions to allow the company to operate more efficiently and to reduce any long term liabilities. A three year period of restructuring, using a private sector model was initiated by the new board. The safety record of NBHDL has always been good and all restructuring was done with safety in mind. NBHDL achieved another safety milestone on January 30, 2004 when the employees reached one year without a lost time accident.

Restructuring

A number of restructuring initiatives took place. They are as follows:

- **Labour Costs:**

The cost of labour and benefits amounts to 80 percent of the total operating budget. In 2000, NBHDL had a total of 54 employees on the payroll with an annual payroll cost \$3,563,399.68. Today, following downsizing initiatives, there are 35 employees on the payroll and the annual payroll and benefit cost is \$3,039,403.65. The downsizing program was achieved in a cooperative effort by providing a financial incentive to employees who were approaching retirement. There has been no reduction in the quality of service to our customers and the company is meeting or exceeding all standards of service as set out by the OEB. The payroll today, if no downsizing had taken place, would be in the order of \$4,689,365.64. An effort has been made to contract out work where it is economical. The IT processing function and meter reading are contracted out at a lower price than doing them in house. Students are hired wherever possible to reduce the cost of labour and specialized functions such as engineering and design on new projects is being contracted out. The overhead for engineering was 30 percent 3 years ago and has been reduced to 10 percent and the goal is to achieve a target of 5 percent. The average age of the employees of NBHDL is 42 years old. It is anticipated that 7 employees will be eligible to retire in the next 3 years. In order to maintain a healthy workforce among the line crew, two apprentice linesmen will be hired in 2004.

- **Consolidation of Operations:**

Prior to July 2000, NBHDL had operations at two separate locations in the city. These operations were about 2 kilometers apart and consisted of a corporate office at 1350 Fisher Street which provided administrative and customer service and an operations center at 74 Commerce Crescent which had warehouse space and was a dispatch center for the line crews. The board made the decision to renovate the operations center to allow the administrative and customer service people to be consolidated into one building. This has brought about operational efficiencies and allowed for the corporate office to be put up for sale. The 20,000 square foot building is valued at over \$1,000,000 and has an annual operating cost of \$120,000. Proceeds from the sale are to be directed into a voltage conversion program and infrastructure upgrading, which is part of the five year capital program. The voltage conversion program is expected to reduce distribution losses in the system losses, which are currently passed along to our customers. The infrastructure upgrading is expected to maintain the reliability of the distribution system.

- **Benefits Costs:**

The cost of benefits at NBHDL cover union employees hired prior to October 28, 2002 and retirees for life. The board recognized that this cost, if not controlled and if the revenue remained the same, would bankrupt the company in the year 2007 or 2008. In an effort to control these costs, the benefits for management employees ends when they reach age 65. It is estimated that this decision has reduced the Accrued Benefits Obligation (ABO) over \$720,000 dollars. However, negotiations with the unionized employees to cap benefits at age 65 were not successful in 2002. Following a 14 week strike, where this was the main issue, all current employees were grand-fathered and all employees hired after October 29, 2002 would have their benefits cease at age 65. This reduced the ABO by at least \$360,000 dollars. Efforts continue to control the cost of these benefits, which increased by 16.4 percent this year. It is essential that the problem of the growing ABO be addressed during the next round of collective bargaining, which is scheduled to begin in March 2005.

- **Other Costs:**

NBHDL uses contractors to do work whenever possible. An effort is made to include as many companies as possible in the bidding process and to use non-traditional companies to do work. As an example, Hydro One was the low bidder on a tree trimming contract worth \$125,000 and they performed the work in an efficient and cost effective manner. The use of private sector contractors is proving to be a cost effective method of getting work done in an efficient manner.

Revenue

The main source of revenue for NBHDL is from distribution rates. The monthly service charge for a residential customers at the present time is \$12.84. If NBHDL had applied for full Payment in Lieu of Taxes the rate would have been \$14.02 and if \$750,000 in transition costs are factored in, the rate would have been \$15.15. The distribution rates we are charging our customers are lower than the provincial average by a substantial margin. In addition, NBHDL did not apply for the full Market Adjusted Rate of Return (MARR). Several other local distributing companies in the province did the same in an effort to keep the rates low and simulate economic growth in their cities. The impact of these items is a decrease in revenue of \$1,500,000 in 2004, which can be translated as savings to our customers.

The main source of other revenue for NBHDL is from joint use on poles, work for others and service charges to our affiliates, primarily the services company (SERVCO). SERVCO produces revenue from hot water tank rentals, sentinel lights and fiber optics (rental income from dark fiber). The GENCO and RETAILCO companies have been incorporated but do not generate revenue.

Partnerships

The Board of NBHDL has always recognized the value of belonging to partnerships and the impact that partnerships have on the operating cost of the company. NBHDL belongs to the following groups and is an active participant in all of them.

- The Upper Canada Energy Alliance (UCEA) was formed in March 2000 and the initial purpose was to procure wholesale electric power at competitive rates. There are 10 local distributing companies in the alliance including Newmarket, Vaughn and Markham. Currently, the benefit to NBHDL of belonging to this group is the ability to participate in Cost Allocation Studies, the Provincial Load Research Project, the Demand Side Management Project and the Demand Response Project. An independent consultant who works on behalf of the alliance is guiding these projects and each member contributes their share towards the cost of the consultant. In addition, ideas are shared among the group on a regular basis.
- The Cornerstone Hydro Electric Concepts Group (CHEC) was formed three years ago when 20 small to medium size utilities, with a customer base of 195,000 pooled \$75,000 to form a co-operative venture. Some of the companies involved are Orangeville Hydro, Westario and

Collingwood. The geographical center of CHEC is Mount Forest and meetings are held on a monthly basis. There is a free exchange of ideas and the group pooled resources to submit a generic paper on Conditions of Service. Other successful projects have been the Meter Service Provision where 5 or 6 members share in the purchase of spare parts for a high voltage meter common to all. The long term objective is to become a fully fledged co-operative that would represent over 200,000 customers in the province.

- NBHDL belongs to the Northeastern District of the EDA. There are nine members in total in this group and Greater Sudbury and the PUC in Sault Ste. Marie are the two largest members. Two of the main working groups is the purchasing consortium and the engineering standards committee. Both of these groups meet on a regular basis and both bring value to all the members in the Northeastern District. One strength of membership in this group is that all of the members share the same challenges of operating in the north. The Northeastern District meets with the Northwestern District twice a year to discuss common concerns and exchange ideas and information.
- NBHDL belongs to the Electricity Distributors Association (EDA) which provides advocacy and information useful to the utility. Currently, the EDA is negotiating with cable and telecommunication companies for a higher rate for joint use on poles. This will be an additional stream of revenue to NBHDL. In addition, several insurance packages are purchased from the MEARIE Group at rates that are more competitive than going on the open market.
- NBHDL belongs to the Electrical and Utilities Safety Association (E&USA) and relies on this organization to provide on site training as well as annual certification for several aspects of the safety program. In 2003, E&USA provided training to 6 employees for basic certification and workplace specific hazard training. The annual budget for safety for NBHDL is approximately \$50,000.
- NBHDL belongs to the CHUG Group and this is the group that represents the Canadian HTE Users. HTE is the software used in the billing system and membership in this organization has saved the utility a total of \$106,000.00 in 2003 and 2004, and has helped to provide daily support for the software.

Northern Concerns

The Board of NBHDL recognizes the unique challenges of being a northern utility.

The City of North Bay receives \$975,000 as a dividend/interest payment from NBHDL on an annual basis. The city has committed this money as part of their share towards the capital cost of a regional hospital and funding business activities of non-revenue generating affiliates. This regional hospital will serve people as far north as New Liskeard and the Tri-town area. It will also serve people as far west as the Quebec border (and into Quebec). From the perspective of acute healthcare, North Bay is a focal point in the north and the financial viability of NBHDL is integral to this success.

Because of the geographical location of North Bay, it is often more economical to purchase equipment in the immediate area. For example, hydro poles purchased in New Liskeard are cheaper than those purchased in the Toronto area after the cost of freight is factored in. An effort is made to buy locally if the price is competitive or if the local supplier is also willing to provide adequate inventory for our needs. When contractors are hired for specific projects, efforts are made to use contractors in the north. As an example, a firm in Timmins has been used on several occasions to do engineering work and their price has been lower than local or Toronto based companies.

All face the same weather challenges. In the event of a storm, a reciprocal arrangement exists whereby we assist one another. Fortunately, we have not had to do this very often. During cold weather, the productivity of the crews decreases which becomes a challenge for management and supervisors.

In terms of future growth, NBHDL looks towards the north for business opportunities in terms of supplying services to turn key management of smaller utilities. NBHDL has a critical mass that allows for business opportunities where economies of scale are required to reduce operating cost.

Capital Spending

The spending of capital money to keep the infrastructure up to date and to take care of expansion in the system has always been a concern of NBHDL. The average annual capital spending over the last five years has been \$2.9 million per year. In the five year capital plan for 2004 to 2008, the projected capital spending is expected to exceed \$15 million. Approximately half of this spending will be for voltage conversion which will substantially reduce energy losses.

The source of money for the capital program will be primarily cash flow from operations. The recovery of regulatory assets, which will amount to \$300,000 per year for each of the next four years, can now be directed towards the capital program.

Culture Change

A significant culture change has taken place at NBHDL.

Historically, all engineering work was done in house. The engineering department had 8 full time employees and now there are 2. The bulk of the work is performed by contractors and in order to maintain low costs, several are used. The engineering costs on recent projects have been as low as 5.5 percent, which is well below the industry standard of 10 to 12 percent.

The concept of operating as for a profit organization is reinforced on a daily basis. The focus is on the monthly operating budget. The strategy is to quantify all activities in terms of dollars and to look for ways to reduce the expenses in all areas of the operation. Students are used wherever possible overtime is minimized and managers are required to show their expenditures on a monthly basis to the Board of Directors.

Co-operation with other companies is encouraged at all times. In addition to participation with all of the above named groups such as CHEC and UCEA, cooperation with stakeholders such as Hydro One has improved over the last several years.

Benchmarking is being done to show how NBHDL compares with other utilities of a similar size. A recent benchmarking exercise indicated that the number of linemen required maintaining our facility compares favorably with other utilities in the province.

A change in the management style from the traditional to one where work and responsibility are pushed down into the organization has resulted in productivity gains across the company.

Future Development

Business opportunities with smaller utilities in the area and West Nipissing Energy Services Limited have been identified and are being pursued.

The potential exists to reduce the operating cost by an additional \$500,000 per year. This would involve labour reductions (through attrition or early retirements), use of technology (such as pay-as-you-go meters and increased use of contract and part time labour).

The AS/400 computer system used to do billing for NBHDL is operating at 85 percent capacity and with additional drivers could be utilized for other purposes such as water billing or billing for several smaller utilities.

Enhanced operation of the affiliates such as Servco and Genco will add to the revenue generated by NBHDL.

The City of North Bay is expected to see significant growth during the next 5 years. Future growth rate of 1.5 percent per year for each of the next five years is forecast. At present rates, this will increase revenue by \$1,274,067.00 per year.

Conclusion

- We are concentrating on efficiencies in the operation.
- Customers are happy with where we are going.
- We are employing the concept of continuous improvement to all aspects of the operation.
- The cooperative model from the United States is being pursued by members of the CHEC Group.