



**Woodstock Hydro Services Inc.**

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February 12, 2004

Peter H. O'Dell  
Assistant Board Secretary  
Ontario Energy Board  
P.O. Box 2319  
2300 Yonge Street, 26<sup>th</sup> Floor  
Toronto On.  
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Dear Mr. O'Dell

**Re: RP-2004-0020**

On behalf of Woodstock Hydro Services Inc. I would like to express my gratitude to the Ontario Energy Board for the opportunity to provide our views on such an important issue.

I do however feel compelled to express, as a prefix to this submission, a concern I have regarding the allotted time to prepare this response. Given the complexity of the issue and the need to receive well thought-out and analyzed responses, I feel that the time frame for this consultation is extremely short.

As stated in section 7 of the February 10 staff paper on this issue, the consultation will provide the opportunity to present reactions to specific issues raised in the paper. In consideration of the deadline for this submission it is our contention that insufficient time has been allotted if meaningful detailed responses are the desired outcome.

We trust that the short time frame is an indication that the Board considers this is a first step in what should be a full and detailed debate with opportunity for a full environmental scan of the existing distribution sector condition.

With the aforementioned in mind I have prepared the following brief response to the invitation to provide input.

## **Current Realities**

The staff discussion paper properly states that the electricity sector has experienced major structural development and other challenges over the past few years. Transformation of the industry from its state prior to the Energy Competition Act to the end state envisioned in that legislation has been anything but smooth.

The numerous abrupt changes in public policy regarding the energy sector and the corresponding changes to legislation has resulted in an environment of uncertainty and prolonged transition. The uncertainty has resulted in increased regulatory risk and in turn stymied market activity.

The staggered and halting transformation of the distribution sector has resulted in some abnormal market characteristics that further frustrate the evolution of the sector.

## ***Revenue Requirements***

Local distribution revenue requirements as indicated in the 1999 fiscal period were deemed to be a prudent starting point for rate setting and the LDC revenues were locked in at this level. It was recognized that this approach created “winners” and “losers” amongst the LDCs. This was due to the fact that LDCs had not historically matched their annual cost of service to their annual revenue requirement. Regulatory constraints aside, in reality, the LDCs operated with multi-year spending cycles that fluctuated according to growth or special capital expenditures. Depending where an LDC was on that cycle in 1999, they either locked in at a surplus or a negative revenue stream. Surpluses were quickly used up in preparation for market opening and those in deficit situation were further burdened. The point is that there is an inequity in the current rates across the province.

This was understood to be a transitional anomaly that would be worked out through various corrective measures to be determined later such as rebasing, cost of service studies or performance based regulatory mechanisms. The delays in bringing these corrective actions to bear have resulted in a false economy situation that hampers the LDCs ability to do long range evaluations of assets. This inability frustrates the natural rationalization that was anticipated with the introduction of a performance based regulatory regime. If the long term revenues cannot be assessed properly the risk inherent in sales transactions increases.

The use of revenue streams that do not necessarily correspond to service costs has also frustrated the notion of using the economic evaluation tools of the Distribution System Code to promote economic expansion of the distribution system. Unless we have rates that reflect the cost of service we cannot compare competing evaluations at LDC service area boundaries or properly assess new embedded distribution applications.

## ***Regulatory Acceptance of Efficiency Options***

The staff discussion paper describes various options available to LDCs to gain efficiencies. The current regulatory framework has driven the need to form elaborate corporate structures to provide any kind of economies of scope. These scope opportunities range from simple provision of billing service for other public domain utilities to full multi -utility service companies.

The tension between providing service in the most efficient manner and ensuring both the customer and the shareholder are benefiting from the efficiency gains is a tension that has not been fully explored. The sector would benefit from a full debate on what options are available in the area of convergence and how we can balance the shareholders and customer interest.

An uncertainty exists in the LDC understanding of what would be considered acceptable by the regulator as it weighs the efficiency options available to it. For instance, it is unclear to what degree an LDC can out-source their operational requirements to a third party without disclosure of the third parties return on investment. Can an LDC do a cost of service study when their costs have been bundled into a few line items pertaining to a third party invoice? Are the details of how the third party calculated its costs within the regulators reach? These questions of how the Board intends to ensure the sharing of efficiency benefits between customers and shareholders is a regulatory uncertainty that is slowing the LDCs ability to assess efficiency gain initiatives.

These examples of the current characteristics of the LDC business environment are provided to illustrate some of the barriers to the Darwinian evolution that was originally anticipated with the incorporation of the LDCs. It would be incorrect to draw conclusions as to the effectiveness of the commercially oriented performance based regulatory environment that the ECA was to have created, because it simply has not been put in place yet.

## **Moving Forward**

The Energy Competition Act was proclaimed over five years ago. A lot has happened in those five years. Very little of it was expected. The Ontario Market was compared to numerous other jurisdictions that had traveled the road before us and had advice to offer. We learned a lot from that advice and incorporated much of what we heard.

Perhaps a lesson from the market design initiative is that it is unlikely that we will duplicate another jurisdiction's results if we take the same measures here in Ontario. Improvement efficiency comparisons can only truly be made if the comparators have the same starting point as well as the same end point. A lot more time should be spent establishing exactly what our starting point is before we try to improve on it.

I apologize for the lack of detailed references to the staff discussion paper. The paper contains valuable information worthy of full consideration. I trust the opportunity for the paper's content to be debated will not be lost as this dialogue continues. The Electricity Distributor's Association consultation on this matter is a work in progress and obviously timely. I would expect the information contained in the OEB staff paper to become part of body of work being developed in that process.

I applaud the Ontario Energy Board for seeking input as it strives to fulfill its mandate. As previously mentioned I trust this consultation is a first step in a thorough examination of the issue. This initiative should assist in providing the OEB with an understanding of the complexity of the issue and the magnitude of the debate that will be required as we move to establish, with clarity, a long-term policy for this sector.

Respectfully Submitted

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