

**EXCERPT FROM THE MAY SUBMISSIONS OF**  
**THE SCHOOL ENERGY COALITION**

**2.4 Density Driven Classes**

- 2.4.1 Aside from the divisions of classes based on volumes, we believe that the Board should consider creating customer classifications based on density. In our view, this is an important cost driver whose exclusion from the rate design process would result in urban customers explicitly subsidizing rural customers. While the Staff Paper [fn. On page 20] appears to propose that this is an appropriate subsidy, we disagree with that implication. As we have recently seen in the Hydro One harmonization process, this can be specifically unfair to identifiable groups, of which schools are one example.
- 2.4.2 It appears to be accepted by distributors, intervenors, and other stakeholders, and by Board Staff, that density is a material cost driver for distribution service. In fact, the Board has recently seen, in the PEG Report “Benchmarking the Costs of Ontario Power Distributors” that customer density is a key variable needed to fairly compare LDCs. With the evidence available to the Board, there can be little doubt that it costs significantly less to serve customers in higher density areas than in lower density areas.
- 2.4.3 In our submission, once the Board identifies a material cost driver, the Fairness Principle dictates that, through rate classes, rate structure, or billing determinants, that cost driver should be reflected in rates and therefore in the bills paid by customers for the service. That is the essence of cost causality. There should be only rare occasions where a material cost driver is not part of the structure of rate design.
- 2.4.4 Here, it is not disputed, we think, that the density cost driver can be captured in a number of ways, of which the simplest may be the method used by Hydro One, ie. separate customer classes for rural and urban customers. While there are issues with where the line should be drawn, and what the best metric might be, those are matters endemic to all rate design analysis. They are eminently solvable problems.
- 2.4.5 But Board Staff appear to have rejected density-driven classes for a different reason. From the Staff Paper, it appears they believe there is a policy reason for urban customers to subsidize rural customers. With respect, we disagree with that conclusion, for three reasons.
- 2.4.6 ***Social Policy Issue.*** If there is any policy reason for such a subsidy, that policy would be a social policy, not a regulatory policy. That is, the reason would not have anything to do with the efficient functioning of the electricity sector. It

would have to do with the most efficient social matrix within Ontario society.

- 2.4.7 Allowing benefits to flow from urban dwellers to rural dweller in our society could well be a very good social policy, and it is in fact one that governments often engage. However, the key here is that it is governments that make those decisions. This Board does not have a mandate to engage in social policy. While in light of recent court decisions it certainly has the jurisdiction to consider social policy in its regulatory activities, that is generally not the Board's role, and it has wisely stayed out of social engineering when parties have urged it upon you.
- 2.4.8 We therefore believe that, if it is appropriate for urban dwellers to subsidize the distribution rates of rural dwellers, other than for reasons of sectoral efficiency, we believe that social policy decision should be made by the government, at which point the Board would follow it.
- 2.4.9 ***Customer Sub-Group Unfairness.*** It now appears clear that some customer sub-groups, of which schools are one, are disproportionately affected by such a policy. Any sub-group that is more likely to be located in a higher density area – schools, hospitals, small businesses, etc. – will, if there is no density distinction, be asked to pay more than their fair share of LDC costs so that some other customers, usually residential and large industrial, can pay less.
- 2.4.10 It might be argued, for example, that if residential customers are randomly urban or rural, having some subsidize others is not unreasonable. It is the normal randomness/lack of homogeneity that is to be expected in the composition of any rate class. But, if the class structure includes a systematic bias against a major identifiable customer sub-group, that is a symptom of a fundamental design flaw. Just to give an example, if all general service customers (residential and otherwise) were included in a general service class, with a fixed charge of \$100 a month, residential customers would justifiably complain that they were subsidizing non-residential. We believe that the current subsidy by urban general service customers of rural general service customers is equally unacceptable.
- 2.4.11 ***Evolution of Distribution Sector.*** The problem is exacerbated in Ontario because of how the distribution sector has developed. With many munis to being with, and then consolidation that was based on individual business and political decisions (by the munis, and by the politicians running their municipal shareholders) rather than on the basis of any sound policy strategy, the geographical boundaries of utility franchises do not follow logical patterns.
- 2.4.12 The result of this evolution is that some LDCs are all urban (e.g. Toronto, Ottawa, London, Enersource), some are all rural, and some are mixed. In the case of the former two categories, urban/rural cross-subsidization cannot occur to any significant extent, because the same distributor does not have both types

of customers. But, in the case of the mixed utilities (there are many), their urban customers will pay more so that their rural customers can catch a break.

- 2.4.13** We believe that it is inherently unfair for schools in Belleville or in Orangeville to have much lower distribution bills than schools in Ancaster, or other towns lumped together with rural areas, despite the fact that they have a very similar actual cost of service. If the costs they cause for their respective utilities are similar, in our view their bills should be reasonably close, too, allowing for differences in the efficiencies and policies of individual LDCs. It is unreasonable, in our view, to ask some of those customers, who by an accident of evolution of the sector are in the franchise area of a utility with rural customers, to subsidize those rural customers, while most other urban LDC customers (in Toronto, Ottawa, etc.) are not asked to subsidize rural customers.
- 2.4.14** We want to make clear that it would be a legitimate government policy decision for urban ratepayers to subsidize rural ratepayers. In fact, Rural Rate Assistance goes partway there. But if that subsidization is a social policy decision, it still remains for the Board to implement it in a fair manner. Having some urban customers paying extra, but not others, and for no reason other than historical anomaly, is not consistent with fairness.
- 2.4.15** We therefore recommend that the Board adopt density-based rate classifications. Customers in the cities and towns should have their own separate costs pool, and so would generally pay lower rates, while rural customers would pay the higher rates that their costs justify. The Hydro One structure (although not necessarily their density definition) may be a good starting point to design classes with this in mind.