

THE ONTARIO ENERGY BOARD FINANCIAL REVIEW REPORT

NOVEMBER 2020

SUBMITTED TO:  
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## **Mandate:**

Over the years the OEB has gone through various stages of evolution and governance. The most recent evolution came about as a result of the Ontario Energy Board Modernization Review Panel (The Panel) report of last year. This Report had many significant recommendations, not the least of which guided the governance changes made by the Government to the OEB. In addition, The Panel called for a financial review, which was reinforced by the Minister in his Mandate Letter to the Chair.

As requested in the Minister's Mandate Letter and as an important element of the OEB's modernization, the OEB has commissioned a high level assessment of the financials of the OEB and the financial implications of the OEB on the Energy sector.

## **Approach:**

This high level analysis was conducted over a 4 week period. It involved reviews of available financial material; presentations provided on best in class regulators in the Energy sector; internet research; interview with the Deputy Minister of Energy, Northern Development and Mines; interviews with the Board Chair and CEO of the OEB, interviews with OEB senior staff; and, interviews with CEOs and leaders of selected regulated entities.

This Report will provide a high level "roadmap" which will hopefully contribute to the OEB's upcoming 2021/24 Corporate Plan and to further the modernization plan that the CEO and Board of Directors will undertake over the next three years, largely guided by The Panel's recommendations.

## **Background:**

Regulations and regulators fulfill a vital role in society and the economy. However, given the rapid deployment of technology and change in our economy, the role of the regulator must also change and adapt to these rapid changes and shocks in our society and economy. As a result, Regulators must also anticipate the needs of their shareholders, stakeholders and those that they regulate.

The Energy sector in Ontario, Canada and globally has volumes of material, policy prescriptions and a variety of reviews that have been undertaken over many years. For example, the OECD has researched, benchmarked and written extensively on regulators, regulations, policy and the nexus among these. So, for purposes of brevity and to reduce duplication of these very many excellent studies and analyses I will not summarize nor repeat them here.

The Ontario Energy Board Modernization Review Panel (The Panel) reviewed many of these notable studies and examples of best practices. Moreover, it did a very good job of defining the recent regulatory and mandate history of the OEB in its Final Report to the government:

“The Ontario Energy Board (OEB) is the independent economic regulator of Ontario’s energy sector; its core purpose is to regulate Ontario’s energy utilities in the public interest. The OEB is empowered by statute to (among other things) set rates for regulated entities, license market participants, review/approve consolidations, and grant leave-to-construct applications. The OEB undertakes its role primarily through quasi-judicial processes, reviewing utility applications through formal hearings and issuing legally binding orders.

Over the past 20 years, in addition to receiving jurisdiction over the electricity sector, the OEB has experienced significant changes in both its mandate and its required operations. These include:

- Balancing regulatory independence with responding to an increasing number of government directives;
- Taking on increased consumer protection responsibilities; and,
- Delivering assistance programs such as the Ontario Electricity Support Program.

This mandate expansion was accompanied by extensive institutional changes:

- In 2003, the OEB became a self-financing government agency with a corporate governance structure led by the Chair/CEO and the Management Committee.
- The OEB’s operating expenses have grown, from \$24.5M in 2004-05 to \$43.8M in 2017-18.
- The OEB’s approach to adjudication has changed: the OEB now makes greater use of part-time Board Members and has increased the range of matters that are delegated to staff for decision-making.<sup>1</sup>

It is within this context of change that the OEB Modernization Review Panel (the Panel) was commissioned. The Minister of Energy, Northern Development and Mines tasked the Panel with providing advice on opportunities to strengthen the governance and operational framework of the OEB in ways that increase the confidence of the regulatory community.<sup>2</sup> This Report outlines the process the Panel used to undertake its review, and its recommendations for opportunities to enhance regulatory excellence in the OEB’s governance and operations.”

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<sup>1</sup> Fiscal Year 2008-09: 315 Decisions issued – 117 by Board Members, 198 by delegated staff. Fiscal Year 2017-18: 323 Decisions issued – 61 by Board Members, 262 by delegated staff. Information provided by OEB September 2018

<sup>2</sup> In The Panel’s Report, Appendix A: Terms of Reference; the Panel defines “regulatory community” as those who participate in OEB processes, including regulated utilities, intervenors, and others who have an interest in the work of the OEB.

Furthermore, The Panel also captures well the future regulatory horizon of the OEB as emerging technologies are starting to mature and take hold in the sector; and, the impacts that this will have on a modern regulator:

“In the process of completing its review, the Panel increasingly appreciated the importance of the OEB’s work. Prudent regulation of the energy sector is not merely about setting fair rates or authorizing capital investments. It is about supporting a growing economy and helping Ontarians maintain a high quality of life. In furthering the adequacy, reliability, and quality of energy service, the work of the OEB supports Ontario’s economic, social, and environmental development.

Given these realities, the role of the OEB will be even more critical over the next decade. New disruptive technologies are poised to impact and redefine the marketplace which the OEB regulates. For example:

- Energy storage facilities such as batteries and other distributed energy resources will increasingly become affordable and accessible;
- Many Ontarians will move towards electric cars; and
- Industrial and commercial customers will seek to generate more of their own electricity, thereby relying less on (and being less willing to contribute to the cost of) the electricity grid.<sup>3</sup>

These and many other changes have the potential to significantly affect traditional methods of generating, delivering, and consuming energy. The resulting new business models, changing consumer expectations, and increased interconnection between the energy system and the broader economy will require the OEB to adapt its policies, governance and practices to continue to serve the public interest.”

This Report has benefitted from the work and recommendations of The Panel; and, the Report’s mandate is informed by the aforementioned requirement in the Minister’s Mandate Letter to the Chair of the OEB.

The OEB has also demonstrated that it has undertaken some improvements over the years to continue to evolve its practices and processes. Most recently, it responded to The Panel’s recommendations by tabling a one year (transitional) Corporate Business Plan for fiscal year 2020/21.

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<sup>3</sup> “Revolution Now: The Future Arrives for Five Clean Energy Technologies – 2016 Update”, U.S. Department of Energy, <https://www.energy.gov/eere/downloads/revolutionnow-2016-update>, “6 Trends Driving Vehicle Electrification in 2018”, Greentechmedia, <https://www.greentechmedia.com/articles/read/how-vehicle-electrification-will- evolve-in-2018#gs.VKAfepk>

In its 2020/21 Corporate Business Plan the OEB has identified priorities for this fiscal year. Some selected examples of those priorities are:

- Proportionate Cost-of-Service Rate Applications
- Review of Reporting & Record-keeping Requirements (RRRs)
- Measure OEB Outcomes

In addition, the impacts of COVID-19 on the OEB's digitization progress has shown marked improvement (e.g. moving to have the Licensing process become digital as well as the Application process); its ability to shift relatively seamlessly to work from home arrangements for staff; and, its ability to undertake virtual hearings in a relatively efficient and effective manner are all indications that the OEB has the ability, when needed, to adapt and do so quickly in support of value to the sector.

The Innovation Sandbox is another example of the OEB trying to provide another means of "testing" regulatory changes and innovations. While it is still in a nascent stage of development and commitment from the OEB, it does hold future promise if implemented effectively.

It is also encouraging to see work underway in the Top Quartile Regulator Project, which was spawned from the recommendations of the The Panel. This Project will seek out best in class practices from other North American jurisdictions and will then determine which practices could be applied to the OEB to address the recommendation of being in the top quartile as a Regulator from The Panel.

The OEB's publishing of certain Key Performance Indicators (KPIs) was a step in the right direction toward increased transparency, especially the changes regarding scheduling for rate cases, delivering decisions within set time limits after all evidence has been heard. In addition, the posting of case schedules pilot project has also been well received.

### **Observations:**

#### ***Context:***

One of the mandate elements of this review is to assess the financials of the OEB Budget for savings and efficiency gains. While this is an important task and demonstrates a move to increased transparency, the bulk of savings to regulated entities and ratepayers will come from the effective review of the processes, requirements, codes and actions of the OEB as an economic regulator of the sector.

This was observed in the Electricity Distributors Association (EDA) August 2019 Report on the Ontario Energy Board Modernization: “OEB regulations and activities materially impact both the cost structure of the electricity system, and the ability of customer-facing local distribution companies (LDCs) to adopt new technologies and to respond to evolving customer expectations.”

Given the size of the OEB in terms of number of FTEs and budget, it should consider how best to leverage other entities and their infrastructure in certain expense areas. It is not sufficient to simply indicate that the OEB regulates the industry and therefore could not leverage any of their spend in selected areas. The governance changes recommended from The Panel position the OEB to take advantage of the scale of other entities (e.g. Ministry) for support or shared service delivery. This will allow for a greater focus on core business activities. There is a posture whereby the OEB maintains independence and its regulatory authority while also partnering to be more efficient.

The Observations in this section are organized under 3 Categories:

- Financial efficiency at the OEB
- Efficiency measures benefitting the Sector
- Investments

### ***Observations on Financial Efficiency at the OEB:***

In almost all organizations there are opportunities for budget efficiency gains. The OEB is no exception. Some immediate observations follow on the OEB’s expenditures. Some of the current expenditures were driven by mandated elements or activities prior to the changes called for in The Panel recommendations.

I would also note that overall there does not appear to be any issues with financial management nor with the relative number of employees. There are a couple of Observations below which address the opportunity to reduce certain budget expenses, among other Observations:

1: “Stakeholder” the Budget on an Annual basis, then finalize through the Board and send to the Ministry. This is done by other organizations in Canada in the sector.

2: The OEB is reviewing, with an objective to improve, its Performance Management Framework in which it captures its metrics and reports on those metrics. There are opportunities in this review to separate output from outcome metrics and to report on results on a more frequent basis.

- 3: Consider introducing an approach that is used by the Office of Gas and Electricity Markets (OFGEM) in the UK, which publishes an annual “Forward Work Programme”. OEB could adapt this to include financial reporting and the modernization efforts it plans to implement in that year under the principles of Independence, Accountability, Certainty, Effectiveness and Efficiency as identified by The Panel.
- 4: The Public Affairs Division’s current spending seems more oriented to external, brand building activities. This does not seem to align with the internal cultural change and regulatory transformation that should be the focus. So, approx \$600K could be repurposed and/or reduced. Some investment in the internet and intranet sites and communications of modernization plans and results should be considered.
- 5: Undertake a detailed review of the use of consultants, in the areas of expert opinions generated for the OEB, external legal services and in back office and policy functions, to ensure that they provide true value add and contribute to capacity building.
- 6: Should consider examining the long term contract for HR Legal advice (\$1.7M) should be examined to reduce costs, especially given the OEB is in the off cycle of negotiations for a Collective Bargaining Agreement; given there are 10-12 grievances only per year; etc... Consider the episodic use of a roster of legal HR resources for advice on any departures.
- 7: It is recognized that a long term lease has just been recently renewed for OEB’s office accommodations, in early 2020 pre-pandemic. However, given the swift move to work from home arrangements due to COVID-19 distancing requirements; the move to virtual hearings; the fact that the space standards are in excess of Ontario Public Service’s standards; and, among other things, the increased application of digitization, the OEB should look at space reductions and lease reductions in order to decrease its spending on this expense at the expiry of the current lease.
- 8: Carrying an operating reserve to fund working capital and for unforeseen in-year costs and/or requirements which the OEB may be asked to take on is a prudent financial management approach. However, over the last 5 years there has been underspending of the OEB’s budget on an annual basis. There are several good reasons for this underspending (e.g. transitional year where various expenses were not realized). Even with these valid reasons the current operating reserve seems to be quite high (approximately \$8M). The OEB has plans to reduce this reserve over the next 3 years (\$500K/year). However, the OEB should consider a deeper reduction over the next 2-3 years to have the reserve settle at \$3M. A reduction of \$1M to \$2M in each of the next 3 years would allow for the implementation of any required changes to financial processes and would help to ensure that the financial impact of the reduction to \$3M is smoothed over time. This combined with a conservative underspending of say \$1M in any given year seems to be achievable and a good signal of self prudence to regulated entities and ratepayers.

9: Encourage the examination of structural organizational elements of the OEB to determine if they are optimized.

***Observations on Efficiency Measures Benefitting the Sector:***

Substantive changes to the adjudicative process, its requirements, etc... will yield far more in cost savings and additional value to regulated entities and ratepayers than cost savings on the OEB's budgetary spending of approximately \$45M. It is important to address both the OEB's spending and changes along the path to being a top quartile regulator. Therefore, this section provides observations on areas where the OEB could update requirements; tighten processes; and, undertake appropriate changes.

10: Over the 3 year modernization journey, conduct a comprehensive review of all procedures, processes, rules, codes and requirements, with a goal of increasing efficiency within the adjudicative process; reducing the costs of rate filings; and, delivering increased value to ratepayers. In addition, it should also examine various thresholds (e.g. leave to construct thresholds need to be updated to reflect current costs to construct).

11: Assess assertive case management models for their applicability in adjudicative hearings for the OEB, for example:

- more effectively managing Issues Lists generated during rate application reviews;
- be more deliberate about managing In Scope requirements;
- assess cross examinations based on their relevance to directly informing an adjudicative decision;
- consider a more strict definition of who is impacted by a project;
- track duplicative requests and cluster together for efficiency, if possible.

12: Assess legislative requirements for the OEB's role in ensuring Environmental Assessment processes have been followed in capital applications. If this is not legislatively required, then a harmonization opportunity with the relevant Ministry should be explored and communicated as a revised process to regulated entities.

13: At times there may be a reluctance to engage with an applicant in advance of an Application as it would be seen to prejudice the adjudicative decision. However, there needs to be the "space" to have these types of dialogue, without prejudice to any future decision.

14: The Innovation Sandbox present an opportunity to more effectively explore regulatory innovation and transformation. While it is a nascent concept, it also would benefit from being elevated in its prominence in the organization and properly resourced to be able to have genuine dialogue and as a means to drive innovation. A meaningful mandate should be applied for the next 2 years which would need to demonstrate innovations that increase value to the sector and ratepayers.

15: The OEB has already begun an initiative to respond to the Panel’s recommendation of being a top quartile regulator, entitled: the Top Quartile Regulator Project. This is a positive sign and it should be able to demonstrate that the OEB is in or has arrived into the top quartile among global regulators by “ranking” itself against best practices; publicly report the findings; update transparently its journey to being in the top quartile; and, zealously implement the changes and continuous improvement necessary to reach that goal. This assessment and its results should also be a guide for internal transformation for the OEB.

16: In addition, the OEB should consider benchmarking all key administrative functions and costs against other regulators; set public targets to achieve future cost savings and commit to a set of improvement to be delivered over the next 2-3 years.

17: Increase the clarity of when delegated decisions are triggered to improve the sector’s understanding of their use. In addition, consider increasing the use of delegated decisions especially for applications that are less than inflation, e.g. quarterly rate adjustments (pending a review of the legislative implications of doing so).

18: Consider what filing information could be re-applied in a subsequent hearing (e.g. cost of capital), with the objective of examining and reducing the total cost of rate filings.

19: Given that approximately one half of all LDCs are small (by OEB’s definition), consider whether they still need to file a capital plan every 5 years. Perhaps this timeframe could be extended thereby decreasing filing costs.

***Observations on Potential Investments:***

When considering whether one should make investment in various areas of an organization there needs to be a clear understanding of the return on that investment and its contribution to enhanced value to the sector.

20: Consider increasing the amount allocated for training for employees. The types of training that could be considered would be in leadership skills, emerging technologies and change management. This should build on the HR talent management plan of the OEB.

21: Research and assess the future application of blockchain solutions perhaps for authenticating data and addressing the likely impact on the industry as energy technologies continue to evolve and rapidly get more “local” (e.g. microgrids). Or, to be able to better assess the impacts of crypto currencies; the Internet of Things (IoT) devices and their impact on the grid; impacts on time of use; role of aggregators; future development of smarter energy grids; etc...

**Conclusion:**

Over many years the OEB has demonstrated that it is capable of adapting and amending its practices and processes to meet the changing demands of the industry; varying mandates given to it; and, responding to various reviews of its role in the sector.

As chronicled well in The Panel report, and adopted by the government, the appropriate governance changes separating administrative from regulatory functions provides a strong foundation to act on these Observations. Moreover, the need for further modernization of the OEB is required, especially in light of the energy technology landscape and the need to continue to provide increased value to the sector and ratepayers while delivering regulatory decisions for a reliable and sustainable energy sector. Maximizing on the delivery of these objectives provides many opportunities for modernization in the months ahead.

This Report has tried to provide some observations and suggestions (a “roadmap”) for further modernization initiatives to contribute to the OEB being a top quartile regulator.