

January 25, 2021

Christine Long  
Registrar  
Ontario Energy Board  
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Dear Ms. Long:

**EB-2020-0133 – COVID-19 Deferral Account Consultation – CCC Submissions**

Please find, attached, the Submissions of the Consumers Council of Canada regarding the above-referenced consultation process.

Yours truly,

*Julie E. Girvan*

Julie E. Girvan

CC: All Parties

## SUBMISSIONS OF THE CONSUMERS COUNCIL OF CANADA

### RE: ONTARIO ENERGY BOARD COVID-19 DEFERRAL ACCOUNT CONSULTATION

EB-2020-0133

#### INTRODUCTION:

On March 25, 2020, the Ontario Energy Board (OEB) established a deferral account (the Account) in which electricity and natural gas distributors may record incremental costs as a result of the ongoing COVID-19 emergency, the severity and duration of which was uncertain at the that time. The OEB ordered the establishment of the Account along with three sub-accounts for both natural gas and electricity distributors to use to track any incremental costs and lost revenues related to the COVID-19 emergency. On April 29, 2020 the OEB confirmed that the account applied to Ontario Power Generation (OPG) and electricity transmitters.

In April the OEB indicated that the Account could be used to record temporarily foregone distribution revenue associated with the postponement of the implementation of May 1, 2020 rates.

On May 14, 2020, the OEB commenced a consultation process to consider issues related to the Account. As noted by the OEB:

Further detailed accounting guidance, including policy direction, will be required to be issued by the OEB on key issues in order for rate regulated electricity distributor, transmitters, natural gas distributors, and OPG to be able to assess the need for, and if necessary, properly make applications for review and disposition of the Account balance in due course such as:

- Rules on the operation of the three sub-accounts;
- The nature of the costs/revenue to be recorded;
- Timing and recovery (including the nature of any near-term relief, if needed)
- How materiality will be assessed;
- Whether any additional revenues or offsetting cost savings need to be considered; and
- Rate impacts and rate mitigation consideration.

The objective of the consultation is to assist the OEB in the development of new accounting guidance related to the Account and filing requirements, where appropriate, for the review and disposition of the Account, giving due regard to bill impacts on customers.<sup>1</sup>

The OEB held a stakeholder meeting on May 28, 2020, and sought comments on its Draft issues List. On July 17, 2020 the OEB determined that future consultation would be assisted by a preliminary proposal to be prepared by OEB Staff (Staff Proposal). On September 24, 2020, the OEB announced that it had retained London Economics International LLC (LEI) to undertake a number of studies to inform the OEB Staff Proposal. On December 16, 2020, the OEB released the Staff Proposal and the LEI studies that informed the Staff Proposal. The OEB Staff Proposal and the LEI reports were both comprehensive and informative, with due consideration to context and options.

OEB Staff has set out that the purpose of the Staff Proposal is to provide OEB Staff's initial views on the scope of the Account and to facilitate and focus stakeholder comments. Furthermore, the Staff Proposal strives to strike a balance between ratepayer interests while having regard to the nature of the COVID-19 pandemic, as well as the assessments provided by LEI.<sup>2</sup>

On January 14, 2021, the OEB held a stakeholder session to allow stakeholders to ask questions regarding the Staff Proposal and the LEI Reports. The OEB has allowed for further comments from stakeholders. These are the submissions of the Consumers Council of Canada (Council) regarding the Staff Proposal.

The Council acknowledges that with COVID-19 we are going through unprecedented times. Recent events have imposed hardships on Ontario residents, business, industry, public institutions and all levels of government. The OEB, in establishing the Account recognized that there may be impacts, as well, on the regulated entities in Ontario. To be clear, at this point the OEB has simply established the Account and sub-accounts to "track any incremental costs and lost revenues related to the COVID- 19 pandemic".<sup>3</sup> The OEB has not yet defined what costs and revenues should be tracked, nor has the OEB indicated whether the entities it regulates should be given any form of relief related to the increased costs and lost revenues arising from the pandemic.

The OEB has a number of objectives set out in the Ontario Energy Board Act, which it is mandated to pursue. These include the following, which are relevant to the OEB's consideration of the matters which are the subject of this consultation:

- To inform consumers and protect their interests with respect to prices and the adequacy, reliability, and quality of electricity service;

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<sup>1</sup> OEB Letter dated May 14, 2020 – EB-2020-0133

<sup>2</sup> OEB Staff Proposal, dated December 16, 2020, p. 1

<sup>3</sup> OEB Letter, dated March 25, 2020



- To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry;
- To inform consumers and protect their interests with respect to prices and the reliability and quality of gas service;
- To facilitate the maintenance of a financially viable gas industry for the transmission, distribution and storage of gas.<sup>4</sup>

The OEB is required to set just and reasonable rates having regard to these and other objectives. The Council submits that the OEB will ultimately be required to find a balance when considering how to assess the impacts of COVID-19. It is required to set just and reasonable rates, protect the interests of consumers and to facilitate the maintenance of a financially viable electricity sector.

The Council notes LEI's observation, which was also referenced by OEB Staff, "although utilities have seen negative revenue and cost pressures as a result of the pandemic, the observed financial impact has so far been controlled". Based on publicly available information, these negative cost and revenue impacts have not translated into acute financial issues for utilities thus far, and data available to date suggests the sector as a whole has maintained its financial integrity<sup>5</sup>.

The Council will set out below its views regarding the Staff Proposals. Overall, the Council is of the view that only in cases where the regulated entities can demonstrate their financial viability is in jeopardy should they be permitted to recover the net costs arising from the COVID-19 pandemic. We believe this is consistent with OEB Staff's view that utilities must demonstrate a financial need for recovery of amounts in the Account, although our approach differs from that of OEB Staff. In this context we see recovery of the amounts recorded in the Account as the exception, not the rule. It is frankly difficult to understand why utilities that are making a profit (any return) should be seeking relief from their customers for costs incurred or lost revenue because of the pandemic. The OEB will clearly have to determine how to assess financial need, and determine when it is appropriate to allow recovery to address that financial need.

#### **OEB STAFF PROPOSAL:**

OEB Staff has set out a summary of its key positions:

- Utilities must demonstrate a financial need for recovery in the Account, subject to certain conditions;

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<sup>4</sup> OEB Act, 1998, Part 1, December 2020

<sup>5</sup> Staff Proposal, pp. 1-2

- OEB Staff suggests a means test based on the lower end of the OEB’s dead band of approved ROE (300 basis points) which ensures that utilities who make recovery claims are doing so to ameliorate the fact that their earnings have been reduced below the point of reasonably expected fluctuations, as opposed to restoration of their full profitability margins;
- For utilities that pass the means test, OEB Staff recommends that any material and prudently incurred incremental impacts, directly attributable to the pandemic should be eligible for recovery at a rate of 50%;
- OEB Staff recommends that incremental impacts (both increases and decreases in costs and revenues) directly attributable to the pandemic should be recorded in the Account. However, utilities should not be required to automatically return any net gains in the Account, in the event that savings exceed costs, as the Account was established to facilitate any claims for relief by utilities at a time when the impact of the pandemic were unknown;
- OEB Staff recommends that only those utilities that have intentions of submitting a claim for recovery (with due consideration to the applicability of the proposed means test) should be required to continue to track the impacts in the Account in order to support their future disposition requests;
- 100% of any prudently incurred and material costs (or lost revenues) necessary to comply with government or OEB actions taken to assist ratepayers should be recoverable in full and the means test applicable to those amounts should be the upper end of the OEB’s dead band of an approved ROE (300 Basis points);
- For the other amounts, in circumstances where utilities can demonstrate that, after passing the proposed means test, their financial viability would be compromised if their pandemic-related recoveries are limited to 50% of the incremental impacts, the OEB should consider recoveries at a rate of greater than 50% on a case-by-case basis.<sup>6</sup>

## CONTEXT:

OEB Staff has stated that the Staff Proposal reflects OEB Staff’s view of what the OEB’s regulatory guidance should be with respect to the nature, purpose, and operation of the Account. Final guidance is anticipated to be issued by the OEB to assist utilities in assessing the need for, and if necessary, properly submitting applications for review and disposition of the Account balance in due course<sup>7</sup>.

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<sup>6</sup> Staff Proposal, pp. 3-4

<sup>7</sup> Staff Proposal, p. 6



The Council is of the view that in determining final OEB guidance it is important to highlight the context in which this guidance will be issued.

At the time the OEB established the Account the OEB it acknowledged that electricity and natural gas distributors may incur incremental costs as a result of the COVID-19 emergency, the severity and duration of which is uncertain at that time. The OEB approved the establishment of the accounts with so much unknown. No one knew what the costs impacts and lost revenue impacts would be. Accordingly, establishing the Account, from the Council's perspective, was the prudent thing to do. That does not mean that the amounts recorded in the Account are necessarily recoverable. There are a number of factors that indicate the impacts on utilities have not been significant relative to the impacts on other sectors of the economy and their customers:

- As noted by LEI reductions of between 6% to 18 % of typical system demand were observed in April 2020 with residential consumption generally increasing and commercial and industrial consumption generally decreasing. Some recovery was observed as restrictions were loosened and temperatures increased during the spring and summer months. For natural gas the direct impact on usage was less pronounced. The ongoing restrictions are unlikely to result in sharp changes to demand as observed following the first wave of the pandemic around April 2020;<sup>8</sup>
- In spite of revenue and cost pressures, the utilities sector as a whole has been comparatively insulated from the pandemic's impact. (Q2 2020 Real GDP change of - 1.3%)<sup>9</sup> This situation has improved since Q2. The electricity distribution revenues were comparatively harder hit;
- Based on publicly available information, observable financial impacts of COVID-19 to date have been controlled, suggesting the sector as a whole has maintained its financial integrity thus far through the pandemic. The impact of COVID-19 on financial health is more observable among larger utilities, but LEI has not seen reports of Ontario utilities subject to financial distress or receiving negative attention from ratings agencies. Negative cost and revenue impacts have not translated into acute financial issues for utilities and the sector as a whole has maintained its financial integrity thus far;<sup>10</sup>
- One specific area of concern going forward relates to liquidity risk that may emerge for utilities (particularly on the distribution side) in the event that negative cost and revenue pressures persist;<sup>11</sup>

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<sup>8</sup> LEI Presentation, January 14, 2020, p. 6

<sup>9</sup> LEI Presentation, January 14, 2020, p. 13

<sup>10</sup> LEI Presentation, January 14, 2020, pp. 13-15

<sup>11</sup> LEI Presentation, January 14, 2020, p. 14

- The cost of debt for utilities has fallen while the cost of equity in the market has risen, but LEI has concluded that Ontario utilities are fairly compensated for risk based on current parameters;<sup>12</sup>
- To our knowledge no utilities have applied to the OEB for immediate relief given current constraints related to COVID-19, nor have they been unable to provide safe reliable electricity as a result of the pandemic;
- Customer impacts from the pandemic have, been significant with unemployment rates more than doubling in May 2020 and commercial and industrial customers facing shut downs, and revenue reduction. Tenants have been unable to pay rents and landlords unable to collect rents. Some government assistance has been made available, muting, but not eliminating these problems.

The Council submits that this context is important. We are not saying that the entities which the OEB regulates have not suffered, and will not be subject to increased costs and revenues going forward. The OEB, however, in exercising its mandate must both protect the interests of consumers with respect to price while ensuring that the financial viability of the regulated energy sector as a whole and the financial viability of the individual utilities are maintained. Although we believe that the Staff Proposal to require utilities to demonstrate financial need with respect to the amounts in the Account is appropriate, we do not believe their proposals strike the correct balance between protecting the interests of customers and the need to maintain financial viability.

## MEANS TEST

OEB Staff is proposing a means test that should be used to determine the recoverability of the amounts in the Account. Staff has concluded that the Account should operate to ensure utilities do not face undue financial hardship, as a consequence of, and for the period that the pandemic and government-issued restrictions to control the pandemic are in force. OEB Staff is of the view that utilities operating within the dead band are effectively managing within a reasonable degree of earnings and therefor have maintained their opportunity for fair compensation.<sup>13</sup>

OEB Staff have proposed a dead band of 300 basis points from a utility's approved ROE. In OEB Staff's view the lower end of the dead band might be the most appropriate comparator for the OEB in determining at what point the utility's cost structure is substantially misaligned from its revenue stream.<sup>14</sup>

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<sup>12</sup> LEI Presentation, January 14, 2020, p. 21

<sup>13</sup> Staff Proposal, p. 22

<sup>14</sup> Staff Proposal, p. 23



The Council is not opposed to a means test to determine whether a utility is eligible to recover some or all of the amounts in the Account. The test, from our perspective is whether the financial viability of the utility is at risk. The Council has the following comments and concerns regarding the Staff Proposal regarding the means test and the 300 basis point dead band:

- An actual ROE that is 300 basis point below the allowed return embedded in utility's rates does not necessarily mean that the financial viability of that entity is threatened. Many utilities operate with much lower ROEs, and have done so for many years, for different reasons, without seeking some relief from the OEB prior to a rebasing application;
- If the embedded ROE is 9% for example, a 6% or even 5% ROE in the context of the current economic environment, does not seem unacceptable and should not necessarily trigger a subsidy from ratepayers. It may also not be an indication of a threat to the financial viability of a utility;
- There is a range of ROEs currently embedded in the rates of Ontario utilities depending upon when their rates were rebased. In effect, a utility with 9% ROE and one with an 8.3% would have different triggers, and different allowable recoveries;
- OEB Staff has proposed that the dead band should act as a threshold and a cap. If the OEB accepts the threshold, then it should also act as a cap. It should not be used as a trigger that allows a utility to recover 50% or 100% of all of the eligible costs;
- OEB Staff has differentiated between net costs resulting from the pandemic and those resulting from government or OEB mandated initiatives. For the costs related to the mandated initiatives OEB Staff proposes that 100% recovery should be allowed. In addition, OEB Staff recovery of these amounts should be based on a means test whereby the utility's ROE does not exceed the upper end of the dead band of 300 basis points from a utility's approved ROE<sup>15</sup>. The Council is opposed to such a proposal. Utilities should be allowed to recover the net costs necessary to maintain their financial viability. Under Staff's Proposal utilities earning 300 basis points above their allowed return would be subject to 100 % recovery of these costs. Based on a 9% ROE embedded in rates a utility would be seeking recovery of these costs from ratepayers while their shareholders are earning a 12% ROE. In the context of the current economic environment and having regard to the OEB's objectives and mandates, this is simply not fair to ratepayers. Utilities should be able to recover a level of these costs that will ensure their financial viability is maintained;
- The Council is of the view that the means test should be based on need. Does a utility need recovery of costs in order to maintain its financial viability? If so, they should be permitted some level of recovery. The Council generally agrees with OEB Staff's

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<sup>15</sup> Staff Proposal, p. 19



proposal regarding causation, prudence and materiality subject to the concerns noted above. The costs that are to be recovered should be directly arising from the pandemic. The utility must demonstrate it acted prudently to minimize the impacts of the pandemic and has fully exploited all available cost reductions. In addition, the amounts recorded in the account for potential recovery should have a material impact on the utility's operations based on established materiality thresholds;

- If the OEB determines that a threshold is required it could set it at 300 basis points or lower (given current economic conditions). This threshold would be simply that. A trigger that allows for an application to be made for some level of cost recovery. In assessing what cost recovery is allowed the OEB should take a wholesale look at each entity on a case-by-case basis. Every utility will have differing circumstances and will be in different financial circumstances. Among the considerations for the OEB would be financial viability in the short term and the long term;
- The OEB should establish filing requirements for the applications that will enable it to assess need. For example, in assessing prudence utilities should be required to indicate whether they have paid dividends to their shareholders, whether they have paid their executives bonuses, and whether they have attempted to refinance their debt, including all affiliate debt.

#### **LOST REVENUE:**

The Council is of the view that any lost revenue associated with the COVID-19 pandemic should only be recoverable in exceptional circumstances. If a utility can demonstrate that their lost revenue is directly attributable to the pandemic it should be a factor for consideration by the OEB in assessing financial need. Currently lost load is a risk that utilities are compensated through the allowed ROE.

#### **ONTARIO POWER GENERATION:**

The Council is of the view that the policy that results from this consultation should not necessarily be applicable to OPG. OPG is unique and the impacts on OPG resulting from the COVID-19 pandemic are far more complicated relative to the distribution utilities. The Council supports an approach that moves the consideration of these issues and a determination of any recovery of net costs to OPG's payment amounts application currently before the OEB.

#### **UTILITY INFORMATION:**

The Council cautions the OEB about making any conclusions regarding the information filed to date regarding Account 1509. The OEB should not base its guidance on the data that has been filed to date, as each utility may be recording things differently. Once filing requirements have been established the data may be more meaningful and of more use to the OEB.

**CONCLUSION:**

The Council submits that the OEB should assess whether Ontario regulated entities qualify for the recovery of costs related to the COVID-19 pandemic on the basis of need. Cost recovery should only be permitted when required to ensure that the financial integrity of the entities is maintained. The OEB should consider each application on a case-by-case basis.

The OEB could establish a trigger mechanism like that proposed by OEB Staff, but the Council is of the view that 300 basis points is too high given current economic conditions. In addition, the OEB should make it clear that potential recovery will be based on a wholesale look at each entity. The onus will be on those entities to demonstrate a threat to their financial viability, and that they have taken all of the necessary measures to mitigate that threat. There must be an appropriate balance between the interests of Ontario ratepayers and the entities that the OEB regulates. In these unprecedented times ratepayers should not be expected to subsidize the returns of the Ontario regulated entities.

**All of which is respectfully submitted.**