



By EMAIL and RESS

Jay Shepherd
jay@shepherdrubenstein.com
Dir. 416-804-2767

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Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
M4P 1E4

Attn: Christine Long, Registrar

Dear Ms. Long:

Re: EB-2018-0287/8 – UR/DER Consultation – Next Steps

We are counsel to the School Energy Coalition (“SEC”). Further to the Board’s letter of January 18, 2021, and the Stakeholder Conference on February 3, 2021, these are SEC’s submissions on the next steps in this consultation.

SEC’s Concerns

The expert reports appear to reach two major conclusions.

First, the impact of Covid-19 is “we don’t know yet, so we can only speculate”. The experts have been quite frank in that assessment, and fairly so. Any “knowledge” of the medium and longer term impact of Covid-19 still awaits a lot more information. The pandemic situation remains fluid, and is likely to continue that way for at least several months, maybe longer.

Second, the future of DERs will largely be driven by price, including both the price of the DER alternatives, and the price of traditional regulated energy supply. While the price of both will be influenced in a material way by environmental concerns, and while some customers will adopt DERs because they are directly motivated to reduce their environmental footprint, DERs will drive significant sectoral evolution mainly as the relative prices of traditional and alternative options themselves evolve. This, by the way, is consistent with longstanding research that price has always been by far the most significant concern of customers relative to their energy suppliers.

While those two conclusions are not earth-shattering, they do confirm SEC in our view of how the Board should look at sectoral evolution, including the impact of DERs.

SEC is concerned with four elements of this evolution, and believes that the Board's approach should reflect a similar amount of regulatory concern for these same four elements. The concerns are:

1. **Stranded Assets.** While the sector is facing significant change, utilities continue to plan and implement capital programs based on a more traditional approach to energy production and delivery. Since utility assets are generally longlasting, and since there is probably general consensus that the sector will be substantially different within the life of those assets now being built, there is a serious risk of stranded assets.

This creates two problems. First, customers are often assumed to be on the hook for capital spending over the long term. As spending creates the potential for rising costs, more and more customers will seek to limit their grid exposure, or exit entirely. This may create a game of musical chairs, in which a progressively smaller group of customers is at risk of being left holding the bag.

Second, for utilities it will be increasingly questionable whether aggressively adding long lived assets passes the prudence test. At the same time, they will be faced with near term needs that do not have traditional solutions other than adding capital. Thus, just as customers are at risk to bear unnecessary costs, so too utility shareholders may experience a growing risk of being required to bear some or all of those costs.

2. **Incremental Spending.** We have already seen, in this consultation and in some rate applications, the suggestion that utilities should spend their way out of this evolutionary process, for example through "grid modernization", monitoring equipment and staff, utility ownership of non-monopoly assets, and many other proposals.

The obvious problem with this approach is that, faced with competition from new entrants that have declining costs, the best response may not be to add costs yourselves. This just increases the price advantage for new entrants, or accelerates the day when they can provide a cheaper and better energy solution for your customers. This attitude on the part of utilities is understandable, since they are by definition in a business that (for the most part) does not have to deal with competition. On the other hand, it may be self-defeating, and in the meantime may add costs to the bills of customers in a futile attempt to deal with that competition.

3. **Utilities Entering Competitive Businesses.** Many utilities – whether they are in the wires or the pipes business – have already said that they would like to be freed up to participate in the market alongside the new entrants. In theory, this may be reasonable, but for two problems. First, utilities operate on a business model that is not driven by risk and innovation, so they are not structured to compete well with their more nimble competitors, especially by offering the same services as those competitors. Second, the utilities would

like to trade on their utility status to lower their risk, essentially competing unfairly with private companies that do not have a government-protected monopoly to fall back on.

From the point of view of the customer, this is a significant problem. Unfair competition increases prices in the market by reducing the impact of market forces. It also puts the utilities at risk, because they are engaged in businesses that are not part of their core competencies. Customers thus are at risk to have weaker utilities for that side of their energy services, and a less robust competitive market for the other side of their energy services. They lose both ways.

4. **Experts Assuming LDC Centrality.** From a process point of view, it is striking the number of times the experts working on this have suggested that the OEB “work with LDCs” to deal with issues. There is a lot more of that than recommendations that the OEB work with customers, yet the assumption of all appears to be that the customers will be the ones paying for sector evolution and the responses to it, one way or another.

It is perhaps unsurprising that experts whose bread and butter is working for utilities will see this as a problem to be solved by the utilities and their regulator. However, given that the intent is to then present the bill to the customers, SEC believes that the customers must be fully represented at the table throughout all aspects of this continuing consultation.

Next Steps - Criteria

Some stakeholders argue that there should be a pause in this consultation, in part because of the pandemic and in part because there is a lot of information still to be gathered before evidence driven policies can be considered. Other stakeholders argue that the time is ripe to push forward with changes to the structure of regulation in this sector.

SEC believes that the question OEB Staff and the Board should be asking themselves is “**What do we need to do now?**” In our view, there are two reasons to do something now:

- a. **Urgency.** There are some components of the evolution of the sector that are already happening. Decisions are being made. Strategies are being developed and implemented. Without prioritizing those components the Board runs the risk of having to develop reactive policies, essentially on the fly. If utilities or private companies or customers are doing new things now, then the Board should be considering now whether and, if so, how the regulator should respond.
- b. **Critical Path.** There are some aspects of sector evolution that, while not immediate, will require some preparatory steps to get to an appropriate policy. SEC believes that, in these cases, OEB Staff should engage in a critical path analysis to identify when a policy will be needed, and what prior activities are required to get there. There are in some cases preliminary investigations (data gathering, for example) that take time and resources, but without which it will be difficult for the Board to develop good policies.

In the analysis below, SEC has tried to identify areas in which either urgency or critical path analysis requires action now, rather than waiting.

Next Steps – SEC Recommendations

With that background, SEC suggests the following next steps in the Board's review of sector evolution:

1. ***Scope and ARC Review Working Group.*** A number of utilities have asked for a review of the Affiliate Relationships Code, with a view to loosening their shackles on leveraging utility resources to enter competitive markets. In some cases, utilities would like to see an expansion of the areas in which utilities can treat competitive activities as if they were monopoly activities, including putting assets into rate base and presenting themselves as better than their competitors because they are the “trusted utility”. Some of the competitive companies support this since, knowing the potential power of a utility brand, they would like to ally with utilities to gain a market advantage over their competitors.

SEC strongly agrees that a review of what utilities can and cannot do, both in the utility and through affiliates, is an urgent requirement. Utilities and their private allies have plans to do this now, and are already pushing at these boundaries. On the other hand, the reason SEC (and perhaps other customer groups) put this at the top of the list is that we believe the restrictions on utilities playing in the competitive markets should be strengthened, not weakened. We believe that the expansion of DERs and therefore customer choice will be supported if the Board ensures monopoly advantages are not used to stifle it.

We therefore believe that a working group (OEB Staff, utilities, customers, competitive players, and other stakeholders) should be established to consider how the Board's policies can best ensure that utilities are allowed to do what they should be doing, and the competitive markets are left to deliver what they do best. This could include revising ARC, but also tightening up the Board's guidance on non-utility activities carried out within the utility.

2. ***Capital Planning Working Group.*** A close second on the urgency scale (perhaps a tie) is a review of capital planning processes and assumptions used by utilities in developing their distribution (or utility) system plans. Ontario's utilities are each year adding billions of dollars of new regulated capital to rate base, almost all based on the traditional monopoly model of energy services. It is unlikely that the utilities will change their approach unless the Board pushes them in that direction. Utilities can only grow, and increase their value and their profits, by adding to rate base. DSPs filed with the Board consistently reflect that imperative.

Driven by SEC's concern with stranded assets, we believe that utilities, their customers, and other stakeholders should work together to develop new approaches to capital planning. The tricky balancing act between immediate capital needs (renewal, reinforcement, etc.) and minimizing long term risks should not be left to the regulated entities (unless, of course, their

shareholders want to take on the stranded asset risk). A working group should be established that has as its mandate the development of approaches to capital planning that protect both current and future customers from excessive costs and risks.

SEC notes that, given the experience of the Board and the parties over the last several years of looking at distribution system plans, this is also an opportune time for the Board to provide some structure and expectations around those plans going forward.

- 3. *Data Sharing Working Group.*** As DERs become increasingly important in the market, information is going to soar in value, not just for utilities and competitive players, but also most importantly for customers. All three groups – utilities, competitive companies, and customers – have information that the other groups would like to see. In each case, there are difficult issues of confidentiality, competitive advantage, and privacy that need to be addressed. On the other hand, DERs will not roll out fully, and customers will not have access to the full advantages of DERs, and the utilities will not be able to properly manage their systems, if this information is not shared to the fullest extent possible

SEC submits that the Board should establish a goal of maximum transparency, with as much information as possible being made available by all participants to all other participants in real time. Customers should know the system constraints specific to their location and load, and the options to deal with them. Competitive companies should know where and how they can add value in any given system, even on any given feeder or pipeline. Utilities should have visibility on supply and load management on their system. In each case, the sharing should be optimized, while at the same time respecting individual rights and avoiding the danger of market paralysis through bureaucracy.

This is a challenging problem, but without this preparatory work the rollout of DERs will be impeded. We therefore see this as a key item on the critical path to a system in which DERs and traditional supply can work properly in tandem. A working group to deal with this should be established now, so that the first step in a solution can be implemented in the next 12-18 months.

- 4. *DER System Modelling Process.*** One of the things that has been striking in this consultation so far has been the range of assumptions people have about the future with DERs. Much of the discussion has speculated on whether expanding DERs will cause or solve this problem or that problem, and what resources utilities and others will need to deal with DERs.

Most of this should actually be discoverable through analysis and modelling. Because many of the impacts of DERs will be driven by physics, not opinion, it should be possible, if clearly non-trivial, to model existing systems with various assumed additions of DERs, based on various price points, etc. Scenarios can be developed, and results of potential technical and policy interventions can be forecast based on science, not guesswork.

SEC classes this initiative as critical path, although it is arguably urgent as well. Lack of system modelling of the impact of DERs means that the Board doesn't have a complete picture of the issues it will be facing in this area. It is perhaps trite to say that knowing the problem is key to dealing with it.

Unlike the other four recommendations in these submissions, SEC does not believe this is a suitable candidate for a working group. We see this as optimally an OEB Staff run process that starts by gathering the system modelling that already has been done, whether academically, in other jurisdictions, or by Ontario utilities. That may already provide enough information to get a firm view of a DER-heavy future in Ontario. If not, further studies can be commissioned to model specific LDCs, for example, for the effects of different configurations of DERs. While not requiring a working group, SEC believes that OEB Staff would be assisted in this by an advisory group that helps them oversee the research and modelling exercise.

5. ***Rethinking Utility Remuneration.*** A number of utilities would like to see additional avenues of profit generation made available to them for pivoting from a traditional model of energy services to a new, more competitive model. This is not just in Ontario. In New York, California, and elsewhere utilities are seeking extra compensation for considering and implementing non-wires or non-pipes alternatives to capital spending. They are also seeking compensation for a new role as managers of an increasingly complex system, with many new players attached to it.

SEC agrees that the time is now to review utility remuneration, but not with a mandate to simply add more utility profit streams. Indeed, it is at least arguable that utilities do not need further incentives to deal with sector evolution. They have to do it in self-defence, so one point of view would be that it is 100% a shareholder expense.

That having been said, the traditional model in which utility profits are driven by rate base may be a dinosaur in a new era in which capital spending is less of a focus. It is likely that the Board should look for new utility business models that provide fair remuneration to shareholders for delivering outcomes valued by customers. If those outcomes are becoming less about poles, wires, and pipes, then the remuneration model should adjust to reflect those new outcomes.

Changing how utilities make money will undoubtedly be a long process, which is why SEC believes that, using the critical path criterion, the Board should start now. A working group should be established to develop options for utility remuneration, and to tie those options to outcomes. This will then allow a debate over the available options, and likely testing of some of them over time. As the nature of the system evolves, it may be possible for the Board to adjust utility compensation step by step, in parallel. While a "new" remuneration model may not be fully implemented for 5-10 years, it is unlikely the Board can even get there unless work starts on this today.



SEC notes that this is not an exhaustive list, and we fully expect that other stakeholders will have suggestions for urgent or critical path activities that should be started. We believe, though, that the five areas listed above should be included in any near term plan for work on sector evolution by the OEB.

All of which is respectfully submitted.

Yours very truly,

Shepherd Rubenstein Professional Corporation

A handwritten signature in black ink, appearing to read "Jay Shepherd".

Jay Shepherd

cc: Wayne McNally, SEC (by email)
Interested Parties (by email)