OEB Legislative & Regulatory Amendments

Update

September 29, 2016

Context

- For approximately two years, the Ministry and the OEB have been in discussions on proposed *Ontario Energy Board Act, 1998* (OEBA) amendments to promote process flexibility and streamline OEB governance.
- These efforts have led to three pieces of legislation: Bill 112, Bill 135, and the proposed Burden Reduction Bill.
  - The Burden Reduction Bill died on the Order Paper as a result of the Prorogation of the Legislature. As of September 21, MEDG has no definitive timetable for its reintroduction but is committed to doing so.
- Before continuing with additional proposal implementation, it is prudent to consider how the OEB is incorporating its new authority into its oversight of regulated entities.
- There are opportunities approaching that will allow for the OEB's role in the electricity sector to be considered in a more comprehensive fashion. These include the Long-Term Energy Plan (LTEP) and the OEB Mandate Review.
- This deck highlights how these efforts can assist in further identifying any potential reforms.

Increased OEB Authority

- Through recent legislation, the OEB's authority and process flexibility has been considerably enhanced. Key measures include:
  - Bill 112
    - Enhanced authority over consumer representation
    - Discretion on division of appropriate regulated and unregulated activities.
    - Expanded emergency management powers
    - Increased flexibility to assess penalties
    - Increased oversight over utility corporate governance and transactions
  - Bill 135
    - Essential role in implementation of the Long-Term Energy Plan
  - Burden Reduction Bill
    - Increased discretion to set policy on customer disconnections
    - Added ability to publish audit and compliance inspection results
- These amendments represent a considerably expanded role for the OEB in terms of sector oversight, and in some cases may require the OEB to provide guidance to regulated entities on how to operate within this new framework.
- The Ministry would benefit from an update on the OEB's capacity and progress in terms of incorporating this new authority into its processes.

Additional Amendments

- There are additional identified amendments that did not proceed through previous legislative initiatives – see Appendix for complete list.
- Many of these proposed amendments require further agency analysis in order to determine if they would serve as beneficial improvements to regulatory authority.
- Prior to moving forward on any additional reforms, it is prudent to consider the OEB's capacity and role in light of the enhanced authority provided to it to date.
- Two upcoming initiatives – **the Long-Term Energy Plan and the OEB Mandate Review** – provide such opportunity as to review the OEB's functions and ensure it is equipped to deliver on its mandate within a dynamic and changing sector.
- The following slides discuss how two identified proposed amendments – enhanced cost allocation and OEB governance reform – can have their complexities investigated through these initiatives.

Cost Allocation

Proposed Legislative Amendment – Cost Allocation

- The OEB has proposed a legislative amendment that would provide the OEB with increased cost allocation discretion across licensed distributors.
- This would allow costs for assets that provide benefits on a regional or provincial scale to be allocated more broadly beyond the customer base of the investing LDC.
- ENERGY and OEB are supportive of initiatives that can drive lower-cost solutions to broader infrastructure needs and promote regional planning. The legislative proposal aligns with stakeholder feedback on ways to unlock the value of specific investments and technologies.
- However, there are a number of complexities and considerations that must be investigated in order to ensure a new cost allocation framework evaluates the benefits of investments appropriately and protects consumers from unnecessary costs.
- The following slides provide an overview of the cost allocation issue and recommend next steps through the Long Term Energy Planning process.

Proposed Legislative Amendment – Cost Allocation

- A long-standing practice within cost-of-service regulation has been to require LDCs to demonstrate that their costs are necessary, reasonable, and offer a net benefit ***directly*** to their customers. This is considered an integral aspect of an independent regulator's consumer protection mandate.
- Under this approach, there is potential for a proposed LDC investment to be rejected where it does not pass a cost-benefit analysis with regards to the LDC's customers, but is a net benefit when considering spill-over benefits that accrue beyond the LDC's boundaries to other sector organizations. This is known as the **diffuse benefits problem.**
  - This could lead to LDCs incurring opportunity costs, system inefficiencies, and investment duplication.
  - In Ontario, the issue is exacerbated by the fragmented nature of the sector. In other jurisdictions, vertically-integrated utilities can create stronger business cases for such investments.
  - This has been a long-standing issue with regards to shoulder-to-shoulder utilities, and mitigation is attempted through regional planning.
- Various stakeholders have proposed that an appropriate regulatory solution would be to assign a benefit value to other electricity sector organizations and implement cost-sharing accordingly (to be recovered through the rates of each affected organization or through charges to other market participants that benefit). The OEB's legislative proposal aligns with this suggestion.
- The diffuse benefits issue has become more prominent in recent years as disruptive energy technologies like smart grid and energy storage have emerged, with suggestions that a failure to address the diffuse benefits issue may prevent Ontario from realizing the full value of grid modernization.

Proposed Legislative Amendment – Cost Allocation: Considerations

- A cost allocation framework that shares costs across regulated and unregulated entities should address certain considerations and risks to ensure consumers are protected:
  - **Valuation of Benefits:** Many of the spill-over benefits are difficult to quantify in monetary terms. An evidence-based framework that assigns a valuation to specific benefits is required for transparent cost-benefit analysis. This was an *Ontario Smart Grid Assessment and Roadmap* recommendation.
  - **Division of Costs:** Determining which organizations benefit from each specific investment (and to what degree) could be imprecise and contentious. As provincial ratepayers will ultimately bear these costs, accuracy in the division of costs will be an important consumer protection consideration.
  - **Verification of Benefits:** The impact and scale of benefits is diluted the further across the electricity system they are assigned, creating challenges in assessing their emergence. A new framework should consider processes that verify consumer benefits from specific investments were realized.
  - **Consumer Preferences:** Investments in improved reliability may result in net cost increases to consumers, justified through quality of service improvements in excess of costs. However, consumers may prefer to forgo added reliability in order to keep costs down. A new framework would need to consider consumer willingness to pay.
  - **Disruptive Models:** Cost allocation could: i) improve conditions for the emergence of new energy business models and services, enabled through disruptive technology, ii) lead to questions surrounding the appropriate division of regulated and unregulated investment, and iii) affect the LDC asset base and therefore profitability, leading to commercial transaction considerations. Changes should be contemplated in the context of the evolution of the sector and what is considered to be in the public interest.
  - **Regulatory Implementation:** Increased cost-sharing has the potential to complicate the rate filing and other regulatory requirements. Process reforms such as joint filings and cost dispute resolution could be considered, while attempting to limit added complexity and burden.
- These considerations, as well as interest from affected stakeholders (regulated utilities, technology companies, consumer advocates), lends evaluation of this proposal to a broader policy development process like LTEP.

Proposed Legislative Amendment – Cost Allocation: Next Steps

- Before moving forward, the Ministry requires further information on what legislative authority the OEB believes is still required.
  - OEB Staff has indicated it has been moving forward on incorporating some aspects of the diffused benefits issue into its regulatory framework.
  - As well, new flexibility under Bill 112 would allow LDCs to bring applications to the OEB that do not align with traditional distributor investment limitations.
- Include discussion of the diffuse benefits problem within the LTEP process, alongside broader discussion of emerging trends and other distributions sector issues.
- Review stakeholder feedback on the diffuse benefits problem and cost allocation options during the LTEP consultation period.
- ENERGY and OEB will then consider options for moving forward in a manner that incorporates stakeholder feedback, including making use of legislative tools to enable a preferred cost allocation framework.

OEB Governance Considerations

OEB Governance Considerations

- In the context of exploring opportunities to refine legislative and regulatory tools that define the OEB's role and structure, there are opportunities to review the OEB that could identify additional reforms.

Mandate Review

- Treasury Board Secretariat (TBS) requires that all Provincial agencies (which includes the OEB) conduct a mandate review once every 7 years to ensure that agency's mandate remains relevant to the goals and priorities of the government, and the agency structure remains most conducive to delivering on the mandate.
- ENERGY has committed to undertake a mandate review of the OEB in 2016-17 through a third party consultant. ENERGY, along with a review team composing of representatives from Treasury Board and Ontario Internal Audit Division, will provide oversight to this review.
- The OEB Mandate Review may be a potential lever to help ensure the OEB is well-equipped to adapt to the new LTEP environment. Recommendations must be reported by ENERGY through TBS and confirmed by Cabinet.
- There are potential opportunities to consider this review in coordination with the effectiveness review which is required by legislation. Under the *OEBA*, the Minister is required to prepare and submit a report to the LGIC on the OEB's effectiveness in meeting the its objectives. The Auditor General has flagged this outstanding issue in various annual reports.

Mandate Review - Scope

- The Mandate Review is not a value-for-money audit nor does the review replace financial or other audits which may be undertaken. The primary aim is to present an objective overview of the agency's function/objective and how best to attain that function/objective prospectively.
- The requirements for a Mandate Review are set forth in the Agencies and Appointments Directive (AAD). They consist of three questions:

  1. Whether, and to what extent the OEB mandate continues to be relevant to the goals and priorities of the government of Ontario?

  2. Is the OEB carrying out the activities and operations as required in its mandate?

  3.Whether all or part of the functions of the OEB are best performed by the OEB, or might be better performed by another ministry, agency or entity?

- The Mandate review can also build off the findings of the OEB's recent AAD audit (see next slide) to explore operational governance considerations more deeply. ENERGY has flexibility to propose additional questions for considerations.
- The final report and accompanying implementation plan, which outlines how best to implement the key results, is expected in by early 2017. Throughout the 3 to 5 month process for the undertaking ENERGY and the OEB will have the opportunity to provide feedback through the receipt of draft reports.
- The results of the review will be tabled before TB/MBC for their approval.

Internal Audit - AAD Compliance Summary

- The Internal Audit Report highlighted many positive developments and substantial compliance with the Agencies and Accountability Directive. The audit did detail some areas in need of improvement wherein both Energy and the OEB could make some adjustments.
  - **Governance** – the audit identified the vacancy of the COO and the combined role of Chair and CEO conflicting with the requirements in the *OEB Act* (and associated risk of compromised objectivity/conflict of interest within the Management Committee) as areas of interest and non-compliance.
  - **Procurement** – the OEB is not in full compliance with the AAD by failing to apply the Contractor Security Screening Directive and the Tax Compliance Declaration Form requirements. In addition, the procurement of the OEB's internal auditor was flagged as inconsistent and including a potential conflict of interest, leading to transparency and fairness issues.
  - **MOU & Business Plan:** Various minor inconsistencies between AAD requirements and the current MOU, including omission of Intellectual Property provisions. As well the OEB Business Plan did not include all risks identified internally by the OEB.
- Internal Audit Division will be holding formal exit meetings with OEB and ENERGY, and will then issue a draft report with recommendations for ENERGY and OEB to comment. Once the final report is issued Internal Audit will report biannually (every 6 months) for two years on the status of the implementation of those recommendations.

OEB Governance – Next Steps

- The Internal Audit can act as a resource for the Mandate Review and LTEP to further expand upon the Board's internal processes. ENERGY and OEB should work together to direct responses on recommendations to these initiatives.
- The Ministry is open to learning more about specific reform proposals from the OEB and how they would lead to improvements in sector efficiency and performance.
- The Ministry will begin the Mandate Review in October, beginning with the hiring of the 3rd party consultant. The final report will be due to the Ministry in Q1 2017.
- LTEP consultations in October/November are an opportunity for stakeholders to express their thoughts on OEB operations.
- Following development of LTEP and the conclusion of the Mandate Review, the Ministry and OEB will work together to identify which governance amendments best serve the customer interest, possibly moving forward through a combination of OEB implementation directive and legislative amendment.

APPENDIX A

Identified Amendments

Status of all proposed amendments

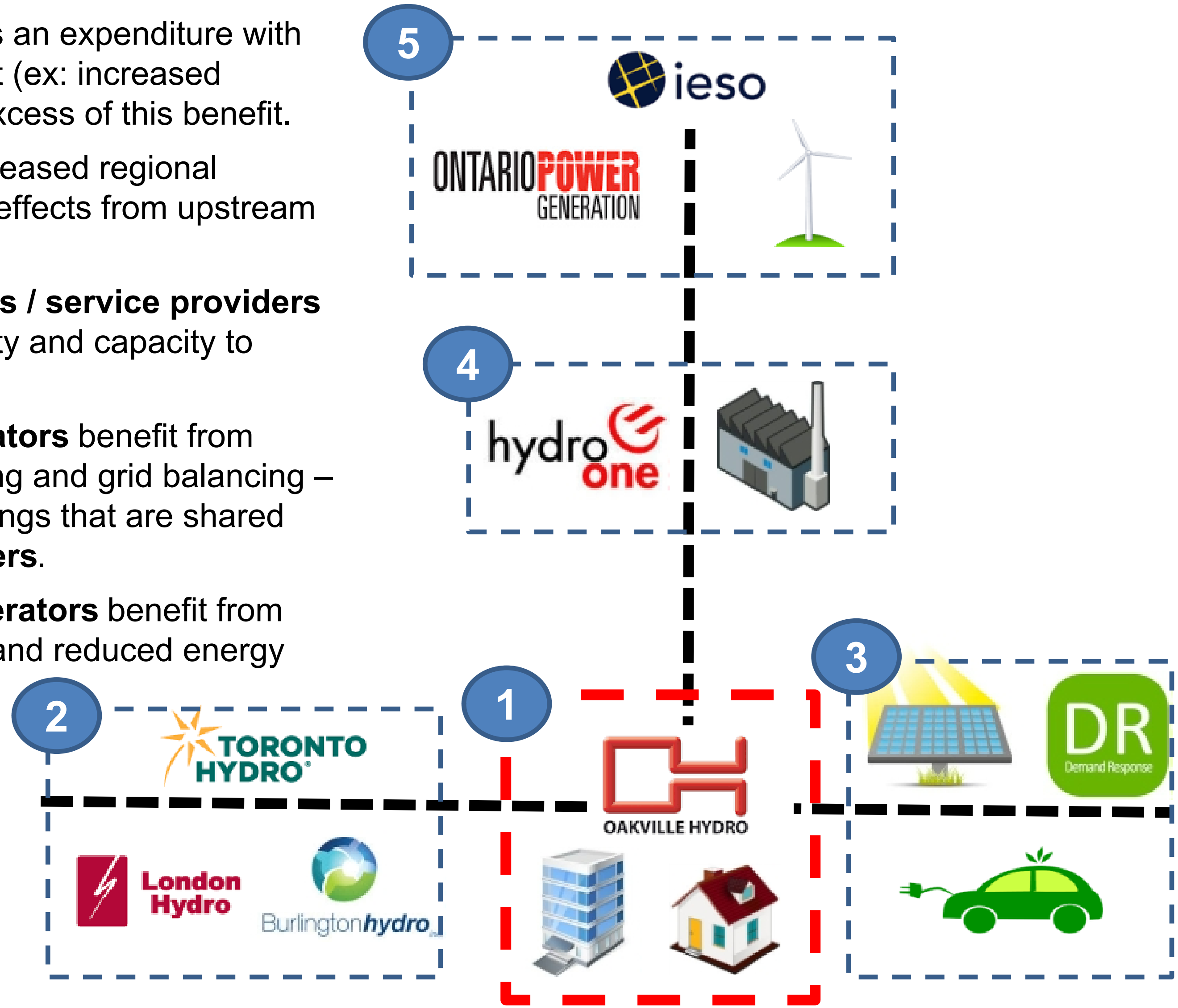
Proposed Amendment/Issue	Status	Vehicle
Permit the OEB to publish audit and compliance results	Burden Reduction Bill	legislation
Increase OEB discretion when reviewing acquisitions involving generators owning transmission/distribution assets or transmitters/distributors owning generation assets.	Burden Reduction Bill	legislation
Confirm OEB authority where liquidator is appointed.	Burden Reduction Bill	legislation
Provide OEB increased authority to establish rules for disconnection.	Burden Reduction Bill	legislation
Extend 60 day timeline for market rule amendment to 120	Burden Reduction Bill	legislation
Greater flexibility in timing of review of deferral and variance accounts	Burden Reduction Bill	legislation
Greater flexibility to determine which investments that connect renewable generation that should be pooled	Burden Reduction Bill	legislation
Correct the definition of "enforceable provisions"	Burden Reduction Bill	legislation
Remove barriers to setting RPP Prices	Posted and tracking for LRC this year	Regulation
Require unit sub-metering providers to pay cost assessments	Ongoing work (Ministry/OEB)	regulation
GEA reporting requirements for LDCs and IESO on connections	Ongoing Work (Ministry)	regulation
Remove spent OPG rebate provisions	Ongoing Work (Ministry)	directive
Ensure OEB Authority is maintained notwithstanding form of business association	Ongoing work (OEB)	legislation
Provide the IESO's Market Assessment and Compliance Division (MACD) with powers of summons, search and seizure.	Ongoing work (IESO/OEB)	legislation
Province wide recovery of distribution costs	Ongoing work that will be part of LTEP (Ministry/OEB)	LTEP legislation/regulation
Oversight of GA allocation and recovery	Ongoing work that will be considered during LTEP.	legislation/regulation
OEB governance structure and regulatory practices	Ongoing work that will be considered during LTEP and the Mandate Review.	legislation
LDC Interoperability – Provide IESO with shared operations of certain facilities	no longer under consideration (issue similar to province wide recovery of assets)	legislation
Oversight of bill presentment	no longer under consideration	legislation
Authorize OEB to grant exemptions to itself and make regulations	no longer under consideration	legislation
ESA oversight of pre-2004 infrastructure subject to OEB discussion with ESA)	no longer under consideration (discussion between ESA/OEB and consensus that MOU, per Bill 112, to be drafted)	regulation

APPENDIX B

Diffused Benefits

Diffused Benefits Across the Electricity System

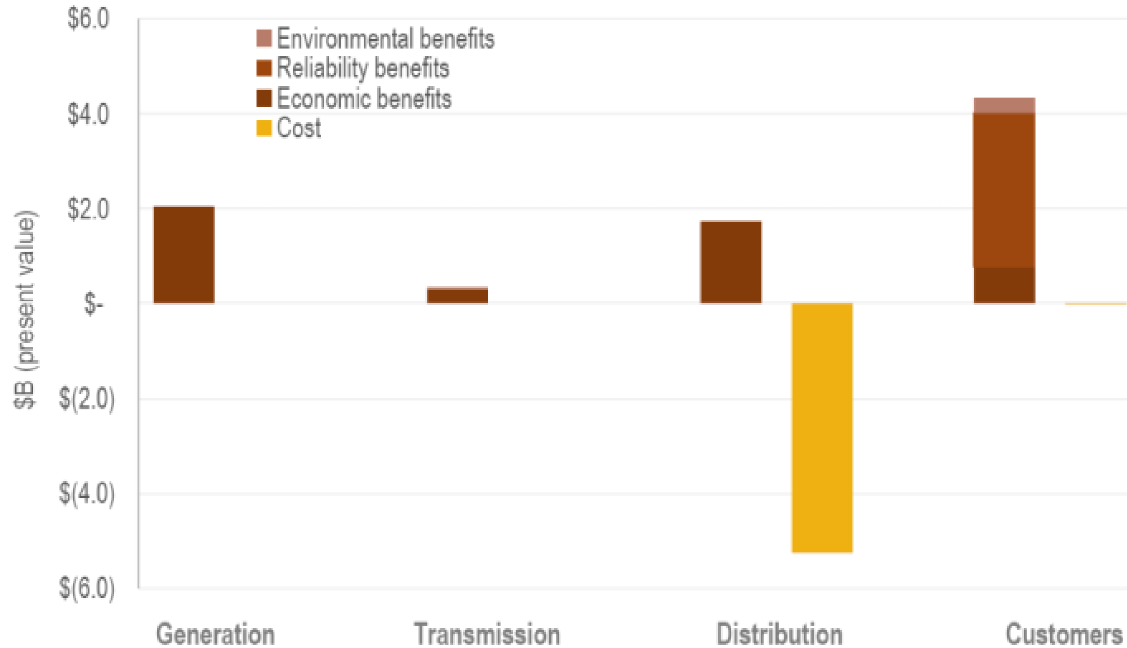
1. **The investing LDC** proposes an expenditure with some direct consumer benefit (ex: increased reliability), but with costs in excess of this benefit.
2. **Other LDCs** benefit from increased regional reliability and/or trickle down effects from upstream benefits, at no direct cost.
3. **Distributed resource owners / service providers** benefit from increased visibility and capacity to interact with Dx system.
4. **Transmission system operators** benefit from improved LDC load forecasting and grid balancing – could lead to operational savings that are shared with **Tx-connected consumers**.
5. **Generators and system operators** benefit from increased dispatch certainty and reduced energy losses.



Diffuse Benefits Example: Distribution of Smart Grid Benefits

- In the ***Ontario Smart Grid Assessment and Roadmap***, Navigant identified that some smart grid investments benefit many electricity sector actors, while the entire cost is borne by LDCs.
- This may create a disincentive for LDCs to engage in smart grid projects with a net benefit to the province.
- By assuming all the expenditures of these projects while not capturing all the benefits, some smart grid projects are a net cost to the LDC.
- This may make an LDC reluctant to engage in such investments and/or the OEB reluctant to approve them.

Figure 19. Distribution of Benefits and Costs for Status Quo Scenario[19]



Source: Navigant; all values in 2014 $ and reflect benefits and costs through 2045.

- Navigant recommended that the government "**consider different approaches to cost allocation that enable the distributors to recover the costs associated with broader system benefits from the wider sector**."
- This recommendation aligns with the OEB request for additional authority to allocate costs across distributor boundaries. However, Navigant's findings suggest the issue should be explored more broadly than simply across LDCs (scope of OEB request) and consider all sector benefits.

APPENDIX C

Details on Proposed Amendments

Amend reporting requirements for renewable connections

- Under the GEGEA, mandatory rules were set for LDCs to facilitate the on-boarding of renewable energy projects; this allowed the OEB to ensure LDCs were connecting projects in a timely manner. This amendment would remove the following mandatory filing requirements of LDCs:
  - number and installed capacity of connection impact assessments (CIA) completed each quarter
  - number of completed assessments that met or exceeded 120 day timeline prescribed by legislation
- The OEB asked whether there is value in maintaining these mandatory reporting requirements given LDCs now have years of experience successfully connecting renewable projects.
  - Each distributor since Q1 2009, has reported a total of 336 data points. The OEB notes that the data collected to date has never been used and suggests that continuing to require the reporting of this data may be unnecessarily burdensome to LDCs.
- Without this requirement, LDCs would still have to report instances where a renewable energy project could <u>not</u> be connected.
- OEB has the authority it needs to be able to impose reporting requirements for any aspect of an LDC’s regulated business as required. As a general rule, a regulation is not required for the OEB to do so. OEB would likely move to an annual rather than quarterly reporting requirement, to reduce reporting by 75 per cent.
- The Ministry supports the amendment and the OEB’s suggested approach.
- While the quarterly reporting requirement does have an administrative cost for LDCs, the OEB cannot quantify the costs associated with mandatory filing. Therefore, the cost reductions associated with the amendment cannot be estimated.
- Posting of the draft amendment on the Regulatory Registry will be required for a period of 45 days. The Ministry will address this in the first half of 2017 following conclusion of LTEP and the Mandate Review, which may identify additional regulatory amendments.

Amend cost allocation regulation to include sub-meter providers

- This proposed regulatory amendment would require unit sub-meter providers to pay an allocation of cost assessments with respect to expenses incurred and expenditures made by the OEB in the exercise of its powers.
  - Sub-meter providers are private companies that provide separate meters for individual units in a multi-unit building, in order to bill for electricity usage on a per unit basis.
  - Sub-meter providers are licensed by the OEB, but the fees that sub-meter providers charge for the provision of sub-metering services are not approved by the OEB. Sub-meter providers are, however, required to conduct their business in compliance with the OEB's Unit Sub-Metering Code.
- Sub-meter providers are a driver of OEB work and should be assessed costs, as is done for other market participants, such as retailers/marketers (who are also not rate-regulated), LDCs and gas distributors.
  - The OEB would be responsible for deciding how to allocate its costs among sub-meter providers (e.g. based on customer numbers and/or complaint information) and has advised that it needs to collect more information internally as well as from sub-meter providers in order to determine a basis for allocation.
  - While the proposed amendment would introduce new costs for sub-meter providers, the specific cost impacts are not known at this time.
  - It is anticipated that sub-meter providers will be resistant to the proposed amendment.
- As this proposed regulatory amendment is made under authority granted by the *OEBA*, it is required to be posted on the Regulatory Registry before proceeding to LRC.
- The OEB may also conduct its own consultation with respect to the method of cost allocation, but would not proceed until the posting to the Regulatory Registry is up.
- The OEB has suggested implementing the proposed amendment as of April 1, 2017 to coincide with the beginning of the next fiscal year. The Ministry will address this in Q1 2017.

Amend Directive requiring OPG rebate provisions

- The Minister issued a directive to the OEB in 1999 under section 28 of the *Ontario Energy Board Act, 1998* (the Act) with respect to licence conditions to address issues which arose from OPG's market share in the Ontario electricity industry. The OPG rebate provisions in the directive authorized funds in excess of the "price cap" set by the OEB on OPG's unregulated assets to be rebated back to eligible customers.
  - The directive has had several updates, with the latest directive (OIC1062/2006) issued in 2006 extending the OPG rebate period to April 2009. The OEB amended the licence conditions as required by the directive accordingly in 2006.
  - Since then, these OPG rebate provisions are included in the OPG generation licence, the Independent Electricity System Operator's licence, all electricity distribution licences and electricity retailer licences. No ministerial directive to the OEB has been issued since the rebate provisions period ended in 2009
- The proposed amendment (or revocation) of the existing ministerial directive would remove the requirement for the OEB to maintain a number of licence conditions with respect to spent OPG rebate provisions that are no longer relevant.
  - Section 28.1 of the Act authorizes the Minister with approval of the LGIC to issue directives amending the directive issued in 1999.
  - Even though the OEB has authority to amend licences under section 74 of the Act, government direction would still be required since the OPG rebate provisions were initially set up by the government through a Minister directive.
- The OEB and ENERGY do not anticipate any policy or cost implications as a result of directing OEB to remove the OPG rebate provisions. This change is considered housekeeping in nature. It can move forward when addressing the other regulatory amendments.
- LSB is working to confirm that a new Ministerial directive (with LGIC approval), the same instrument used in amending the previously issued OICs and directives, would be the appropriate instrument used to revoke or amend the latest directive OIC 1062/2006.

Proposed Legislative Amendments with Agencies

- The two following proposed changes require legislative amendments. ENERGY is waiting for further required input from the IESO and the OEB before a legislative vehicle can be identified.
  - **Provide MACD (IESO's Market Assessment and Compliance Division) with powers of summons and search and seizure (IESO)**
    - IESO and OEB have been working on drafting proposed legislation on this initiative
    - IESO committed to providing a more detailed description and rationale for the enhanced powers requested for MACD. This has not yet been shared with ENERGY.
  - **Ensure OEB authority is maintained - notwithstanding form of business association (e.g. Limited Partnerships)**
    - ENERGY understands that the OEB is working with outside counsel on this issue.
    - OEB and ENERGY need a better understanding of the potential gap in oversight that the proposed amendment is seeking to address.
    - No further details have yet been shared with ENERGY

Summary: Burden Reduction Bill

- MEDG received approval to move forward with its proposed Burden Reduction Bill.
- MEDG will have to reintroduce the Burden Reduction Act due to the prorogation of parliament; the Minister has committed to doing so this session.
- The following eight amendments to the *Ontario Energy Board Act, 1998* and the *Electricity Act, 1998* are included in MEDEI's Burden Reduction Bill
  - Permit the OEB to publish audit and compliance results
  - Confirm the OEB's authority where liquidator is appointed
  - Allow the OEB greater flexibility in timing of review of deferral and variance accounts
  - Allow the OEB greater flexibility to determine which investments that connect renewable generation should be pooled
  - Extend 60 day timeline for market rule amendment to 120 days
  - Increased discretion when reviewing acquisitions involving generators owning transmission/distribution assets or transmitters/distributors owning generation assets.
  - Allow the OEB to prohibit distributors (gas and electric) to disconnect customers during certain times of the year.
  - Correct the definition of "enforceable provisions"