



STAFF REPORT ACTION REQUIRED

Toronto Hydro 2012-2014 Electricity Distribution Rate Application - Ontario Energy Board – City Intervention

Date:	September 27, 2011
To:	Government Management Committee
From:	Deputy City Manager and Chief Financial Officer
Wards:	All
Reference Number:	P:\2011\Internal Services\Cf\Gm11030cf (AFS #14635)

SUMMARY

The City transferred its street lighting assets to Toronto Hydro in 2005, but under the related service agreement continues to pay the cost of the electricity used for street lighting.

Street lighting distribution rates are set based on an Ontario Energy Board (OEB) cost allocation model. The model was created several years ago, but has only recently been phased-in significantly: in 2011 just over 70% of allocated street light distribution costs are charged to the City. Nevertheless, in Toronto and some other municipalities, the phase-in of the allocation model has resulted in a very high cost for electricity, with little ability to avoid costs by reducing power consumption.

On August 26, 2011 Toronto Hydro Electric System ("THESL") applied to the Ontario Energy Board ("the OEB") for permission to increase its delivery charges annually on May 1 2012, May 1 2013 and May 1 2014. In accordance with OEB procedures, on September 26 City staff submitted a notice of intention to intervene in the rate hearing process to protect the City's interests, and are now seeking Council's ratification and approval to proceed with the intervention.

There may be other issues that impact the City which might arise after a thorough review of the application and approval is sought for City staff, through outside counsel, to bring such matters before the OEB.

RECOMMENDATIONS

The Deputy City Manager and Chief Financial Officer recommends that:

1. Council ratify the interim steps taken to date by the Deputy City Manager and Chief Financial Officer and the City Solicitor to seek Intervenor status in the THESL 2012-2014 rate application which is before the OEB.
2. The Deputy City Manager and Chief Financial Officer, the City Solicitor, and outside counsel as required participate in to the THESL 2012 – 2014 rate application and any other related OEB procedures in order to address the proposed distribution rates for the street lighting class and any other classes for which the City is a customer, or any other issues which directly impact the City.

Financial Impact

The 2011 budget for street lighting electricity charges is \$25.5 million, and would rise to \$29.4 million by 2014 under the rate application. If the City's intervention in the 2012 distribution rate application for street lights is successful, the City would not only prevent significant increases in its street lighting electricity expenditures, but could see a significant reduction in costs. For example, a 50% reduction would set rates in line with those paid by some other Ontario municipalities.

The OEB process involves a quasi-judicial hearing and the City will be required to retain external legal and possibly technical representation, with associated expenses estimated to be no more than \$150,000, to be funded from within the 2011 and 2012 operating budgets.

DECISION HISTORY

Toronto Hydro Corporation – Application to OEB to Regulate Street Lighting Assets
<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2009.CC38.21>

ISSUE BACKGROUND

Until 1989, street lighting in Toronto was operated by municipal hydro-electric commissions under the regulation of Ontario Hydro. In 1989, Ontario Hydro required that the municipal hydro-electric commission assets and operations be transferred to the municipal beneficiaries of the service, in order that the related costs would be born directly by each municipality.

In 1999, THESL was incorporated under the *Electricity Act, 1998*. In 2005, the City sold its street lighting assets (over 160,000 streetlights) for \$60 million to its affiliate Toronto Hydro Energy Services Inc. (THESI). THESI began providing street and expressway lighting services on January 1, 2006 under a 30-year Street and Expressway Lighting

Service Agreement. The City pays for the maintenance of and electricity costs associated with the City's street and expressway lights.

Electricity customers are grouped in classes, not unlike property tax classes. In Toronto, street lights are in their own separate customer class, and pay rates different from other classes such as residential. Total electricity charges for street lighting include costs for power consumed (unmetered and estimated based on load profile of bulbs and time of use), regulatory charges, and allocations of transmission and distribution system charges to the street lighting customer class.

The electricity charges for transmission and local distribution are regulated by the OEB. In Toronto, distribution rate applications are submitted by THESL, and these charges have been increasing dramatically in recent years. The rate application process allows affected parties, particularly electricity customers, to intervene in the hearing process and question the basis for the proposed rates.

Also, on August 3, 2011, the OEB issued its final decision allowing the transfer of certain street lighting assets to THESL, at a value of \$28.9 million. As a result, the 2012 rate application also involves related adjustments to the street lighting revenue requirement, which THESL anticipates will be offset by revenues currently paid by the City under the service contract to THESI i.e. with no or nominal net impact on the City. THESL will file additional details by September 30, 2011. City would use its intervenor status to monitor this issue.

COMMENTS

Staff met with THESL in January 2011 seeking a better understanding of the cost allocation model for the street light class. Staff were informed that although there are 42 factors contributing to the allocation of costs, the number of connections between the street lighting system and the distribution system (in Toronto, 1 connection for every 1.8 street lights) dominates the calculation, while the power consumption profile has little impact. As the ratio of connections per light is higher in Toronto than in most other jurisdictions, the allocation model is particularly punitive. In its 2008 rate application, even THESL questioned the allocation methodology¹.

In recent years, the rates associated with this methodology have been phased-in toward full cost recovery (a "revenue to cost ratio" of 1), contributing to a significant increase in the City's street lighting electricity charges. The distribution component alone has increased from \$3.1 million in 2007 to \$15.1 million in 2011, a five-fold increase in distribution charges over four years. The 2012-2014 rate application by THESL incorporates further increases in the revenue to cost ratio from 71.4% in 2011, to 77.9% in 2014, resulting in a forecast of electricity charges as shown in the table below.

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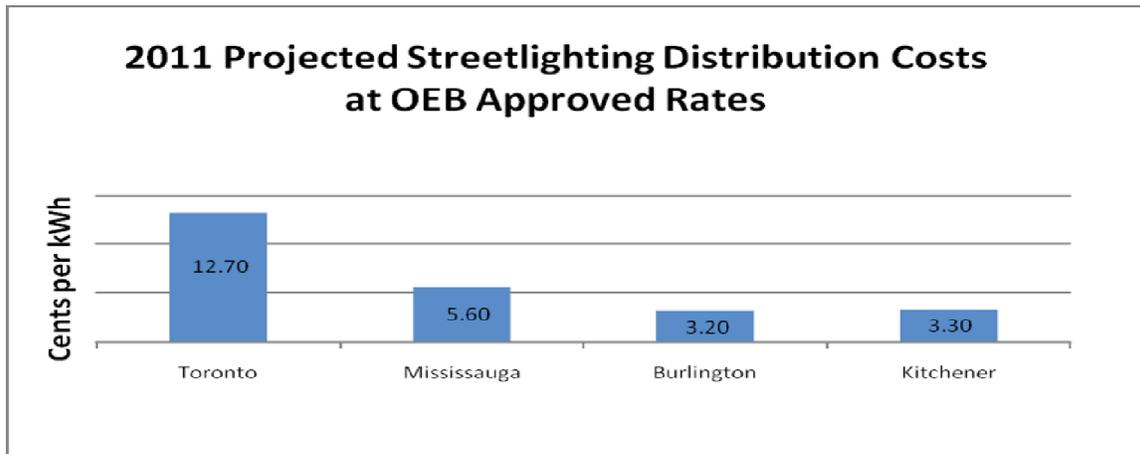
http://www.ontarioenergyboard.ca/documents/consumers/2008edr/torontohydro/THESL_%20Appl_EDR2008_20070803.pdf

**Total Electricity Cost Forecast for Toronto Street Lights
(\$millions)**

Year	2011	2012	2013	2014	2014 Fully allocated costs
Street Lighting Costs (\$millions)	\$25.5	\$26.1	\$27.5	\$29.4	\$37.7
MWh Consumed	118.8	120.0	121.2	122.4	122.4
Cost per kWh (cents)	21.5	21.7	22.7	24.0	30.8
Revenue to Cost Ratio	71.4%	74.0%	76.8%	77.9%	100%

*OEB policy is to achieve a revenue to cost ratio a) within a fairness range of at least 70% and b) progressing toward unity (100% of allocated costs).

These increases will only exacerbate the current situation in which the City already pays a much higher rate for street lighting electricity than some of its neighbours. Based on annual estimated power consumption for the street lights, in 2011 the average cost is 21.5 cents per kilowatt hour (kWh), of which the distribution portion is 12.7 cents. The 21.5 cent cost for 2011 is much higher than typical rates charged for street lighting in other cities, and the 12.7 cent distribution rate is significantly higher than in some neighbouring jurisdictions as illustrated in the graph below.



Toronto is not the only municipality dealing with this issue. In two recent distributor applications in Ontario, the treatment of the number of street lighting connection points was changed, in one case reducing the effective number of connection points and resulting targeted distribution rates being reduced by a factor of five. In a separate OEB proceeding, the Association of Municipalities of Ontario ("AMO") has made arguments for better standards in regard to enumerating connections, the impact they have on rates, and freezing the revenue to cost ratios in the meantime. Staff believe that the City can succeed in making similar arguments in regard to Toronto's situation.

Staff believe that street lights should be charged among the lowest rates of all electricity classes in accordance with their preferred system load characteristics of predictability, consistency, and off-peak (night time) demand. If the City succeeds in having its distribution rates reduced, the cost burden would fall to other customer classes. However, since street lights are a relatively small class (less than 3% of distribution revenue) the impact would be small. Also, a distribution rate reduction would have little effect on the incentive or business case for investment in energy efficient lighting, since these charges are generally not related to power consumption.

Accordingly, staff recommend that Council support an intervention in the rate application and hearing process. Distributor rate proceedings before the OEB are very technical so outside legal assistance with expertise in OEB electricity proceedings will be required. Staff in Facilities & Real Estate, Legal Services, and Transportation Services have been consulted in the preparation of this report.

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SIGNATURE

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