Meeting Notes - #1
Consumer Security Deposit Working Group
Monday, September 23, 2002
9:30 a.m. - 2:30 p.m.

Roy O'Brien (Canadian Cable Television Assoc.)
Melanie Currie (Canadian Federation of Independent Business)
Julie Girvan (Consumers Association of Canada)
Tony Paul (Electricity Distributors Association)
Rita Ronca (Enersource Hydro Mississauga)
Laurie Elliot (Hydro Ottawa)
Brenda Bracken (Hydro One)
Dawn Case (Milton Chamber of Commerce)
Robert Clarke (Milton Chamber of Commerce)
Mary Jo Corkum (Milton Hydro)
John Savage (Ministry of Energy [Observer])
Lisa Marsden (Retail Council of Canada)
John Armstrong (Rogers Cable)
Frank Fabiano (St. Catharines Hydro)
Pamela Tweedy (Toronto Hydro)
Judy Rosebrugh (Wellington North Power)
Chris Cincar (Ontario Energy Board)
Kirsten Walli (Ontario Energy Board)
Martin Davies (Ontario Energy Board)

1. <u>INTRODUCTION</u>

C Introduction of Working Group members as well as a discussion of objectives and process.

2. <u>CURRENT SECURITY DEPOSIT POLICIES</u>

C Brief discussion of existing security deposit policies by LDCs present.

3. <u>ISSUES AND IMPACTS</u>

<u>Local Distribution Companies (LDCs)</u>

Issues

C <u>Previously,</u> LDCs had access to municipal tax roll, the commodity was a predictable *fixed* rate, no IMO prudential obligations, and ability to get rates adjusted by Ontario Hydro. <u>Currently</u>, no longer have access to tax roll, the commodity is a fluctuating *variable* rate and there are significant IMO prudential obligations.

C Ceratin aspects of the current market design are flawed and is the underlying factor contributing to security deposit issues. LDCs are assuming all of the risk, with competitive generators/IMO having 100% guarantee of payment in the absence of any defaults (i.e., if default, into wholesale market “residual risk pool”).[1] Also, under distributor consolidated billing, non-payment risk is shifted from competitive retailers to the regulated LDCs. Only tool available is security deposits from consumers.

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[1] Customers in the retail market contribute to the *wholesale* market “residual risk pool” via LDCs which are wholesale market participants.

- With the introduction of retailers, non-payment risk is shifted to LDC under distributor consolidated billing — 2 separate issues: (1) retailer bankruptcy; and (2) customer of a retailer defaults.
- Cash flow problem due to settlement lag (between when IMO bills LDC vs. LDC billing customer).
- Claims of insufficient bad debts allowance for some LDCs. Is historical data (1999) appropriate under different rules going forward?
- LDC Board members are also still municipal councillors but now have fiduciary responsibility to the LDC OBCA corporations.
- Degree of exposure is an important variable.
- Need for some consistency amongst LDCs.
- Uncertainty of recovery. What is prudent? The introduction of "materiality" makes matters worse.
- LDCs need to have clear guidance/definition on what constitutes "prudence" or "due diligence`` in the view of the Board when determining whether to allow recovery through rates of bad debts in excess of allowance already factored into distribution rates.
- If refund a security deposit after about 5 years of not missing a payment, what if the OEB decides that was not prudent?
- A "tool" to assess each individual customer's risk may be useful. However, LDCs do not have the necessary resources/time to undertake individual risk assessments (i.e., LDCs are not financial institutions).
- "New" customers felt discriminated against, thus, LDC required security deposits from "existing" customers as well. "Existing" customers with good payment history then felt discriminated against.

Impacts

- Increased need to turn to customers for substantial security deposits (only real tool remaining to mitigate risk).
- Credit capacity reduced (i.e., if LDC requires no deposit, LDC is financing the customer).
- Risk of LDC bankruptcy if insufficient security deposits collected from large consumers.
- Cash flow implications (increased borrowing **L** increased interest payments).
- Customer relations on the decline.
- Municipal councillors on LDC Boards must make the financial viability of the LDC the priority. Therefore, can no longer develop or implement LDC policies with economic development as a primary consideration.
- If no security deposits required, IMO prudentials increase. For example, one LDC has $4M in IMO prudential obligations and has only collected $2.3M from customers. The $1.7M difference must be financed by the LDC (i.e., additional interest-related costs).
- Differentiation between owners and tenants.

Customers/Other Stakeholders

Issues

C Concern that large customer will not be required to provide a security deposit. That large customer then defaults which gets included in rates to be paid by residential customers (cross-subsidization).

C There is a need for consistency, with respect to consumer security deposits, across all Ontario electricity LDCs. The current lack of consistency is resulting in inconsistent treatment amongst customers of various LDCs.

C Customers with multiple facilities face different security deposit requirements with each LDC.

C Not all LDCs provide other options **L** only cash.

C Similar security deposits not required in other jurisdictions such as the U.S., Mexico and Alberta. However, other electricity market designs are much different (e.g., no 100% payment guarantee, retailers settle directly with market operator, etc.).

C Never get security deposit back from LDC regardless of payment history (i.e., non-refundable, out-of-pocket).

C Generators should assume some of the risk and not shift it all down to LDCs and their consumers.

C Cross-subsidization between “new” and “existing” customers.

C Security deposit utilizes cash/credit/line of credit capacity; can result in higher interest rate and/or credit crunch.

Impacts

C Cash flow problems for businesses as the security deposit can be about 1/4 of annual electricity bill (all of it in cash).

C Large security deposit could put small companies out-of-business (margins are thin).

C Businesses making decisions regarding where to locate new plants based largely on differing security deposit policy requirements of various LDCs (i.e., pushing businesses to municipalities where LDC does not require a security deposit or to other jurisdictions).

C Large security deposit could have negative impact on Ontario’s economic development (i.e., invest in U.S.).

C New security deposit requirements reduces Ontario’s competitiveness.

C If security deposit never refunded, small business may have to forgo hiring a couple of new staff.

C Competitive implications for business customer of an LDC that requires a significant non-refundable security deposit relative to competitor in another LDC territory that does not require a security deposit at all.

C If bad debts allowance simply increased, all consumers will be forced to pay via higher rates. In contrast, it should be the parties responsible that pay.

4. OTHER MATTERS DISCUSSED

- C Discussion of fairness and equity with respect to security deposits from "existing" large customers (with *excellent* payment history), "existing" large customers (with a *poor* payment history) and "new" customers with no payment history.
- C One LDC described their proposal to create two separate pools comprised of large customers that payed the security deposit (*low* risk pool) and large customers that did not pay the security deposit (*high* risk pool). In cases of defaults by customers that provided no deposit, amounts owed would be collected from only customers in *high* risk pool.
- C A "residual risk pool" that also includes generators.
- C Could require all large consumers to become wholesale market participants (i.e., deal directly with the IMO).
- C Analogy of LDC to a private company (e.g.,GM) not quite appropriate. LDC essentially writing a blank cheque (for duration of settlement lag) and, unlike other products, electricity is not recoverable in cases of non-payment.
- C It was estimated that about 30-40% of LDC load is related to interval-metered customers.
- C Obtaining security deposit policies from LDCs across the province and comparing them was considered. However, security deposit policies of many LDCs are in the midst of being changed and currently on hold awaiting outcome of this process.
- C Working Group agreed that all finalized Meeting Notes should be posted on OEB web site.
- C Ontario *natural gas* LDCs face different circumstances than *electricity* LDCs (e.g., no prudential obligations with organization like IMO, fluctuating commodity price, etc.).

5. NEXT MEETING

- C Tuesday, October 1, 2002
  9:30 a.m. - 2:30 p.m.

Action Items

1) Overview of IMO prudential scheme requested by Working Group members.
Action: **C. Cincar (OEB) to give an overview for Working Group members**.

2) Suggestion was made by a Working Group member to obtain security deposit policies of some Ontario private utilities (e.g., Great Lakes Power).
Action: **C. Cincar (OEB) to attempt to obtain and distribute to Working Group members at next meeting**.

3) Working Group agreed that Meeting Notes should be prepared summarizing each meeting.
Action: **C. Cincar (OEB) to prepare first Meeting Notes.**