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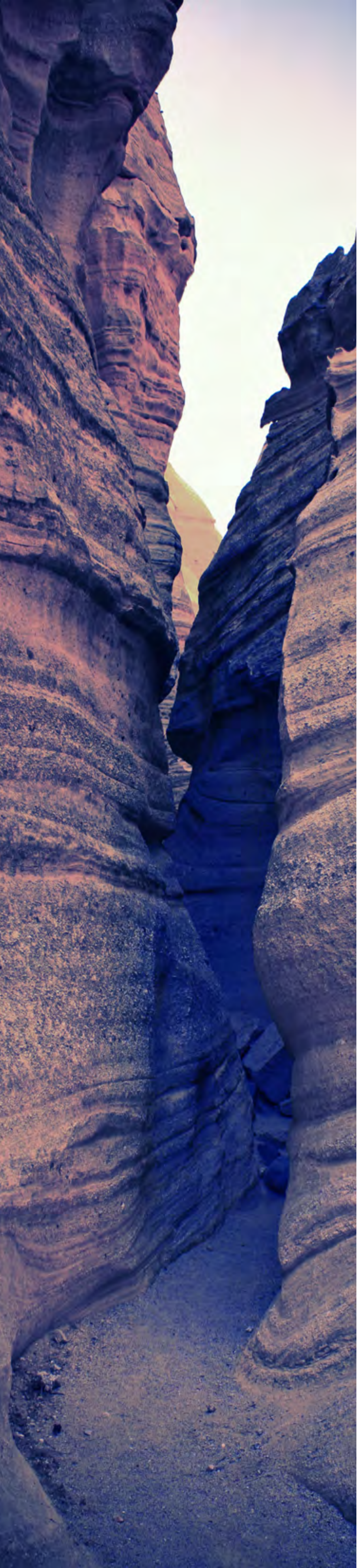
Taking Action in Uncertain Times:

Options for Utilities in Ontario

By John Whincup and Steve Klein

Feeling like you are stuck between a rock and a hard place these days? You're not alone. Many local distribution companies (LDCs) across Ontario are under pressure from shareholders to reduce costs and maximize revenues, and from customers to offer more services and reduced rates (aka the rock). As for the hard place, there are a series of current market pressures that refuse to let up, such as:

- An aging distribution infrastructure requiring significant capital investment but without the necessary funding in place
- Increased productivity demands and regulatory compliance obligations
- Time-bound Conservation and Demand Management targets set by the Ontario Energy Board and directly linked to the LDC's operating license
- The increased rate of departure of skilled labour due to baby-boomer retirements and; Increased competition from renewable energy sources
- Increased share of the cost to operate the electricity power system



Just in case you weren't feeling claustrophobic enough already...

The Ontario government keeps taking away the shovel you need to dig your way out. The Ontario Distribution Sector Review Panel Report—'Renewing Ontario's Electricity Distribution Sector: Putting the Consumer First' renewed the call for less-than-voluntary consolidation in an effort to reduce the cost to Ontario's electricity consumers. The panel had representation from all three parties, suggesting that the push for consolidation will continue regardless of an election outcome.

Furthermore, the inconsistency of policy has been amplified by the appointment of six Ministers of Energy in as many years and the looming possibility of an election has left the sector, and especially the LDCs trying to scrape together any shred of consistent focus.

But don't worry, there are options...

Undoubtedly, the odds are stacked against you, but there is something you can do about it, and the solutions are more accessible than you might think.

LDCs must take advantage of the opportunity to find unique and innovative ways to navigate through these constraints in order to increase their earned revenue potential.

LDCs need to start engaging in exercises that identify potential future options so that they are prepared to take appropriate action when the time comes.

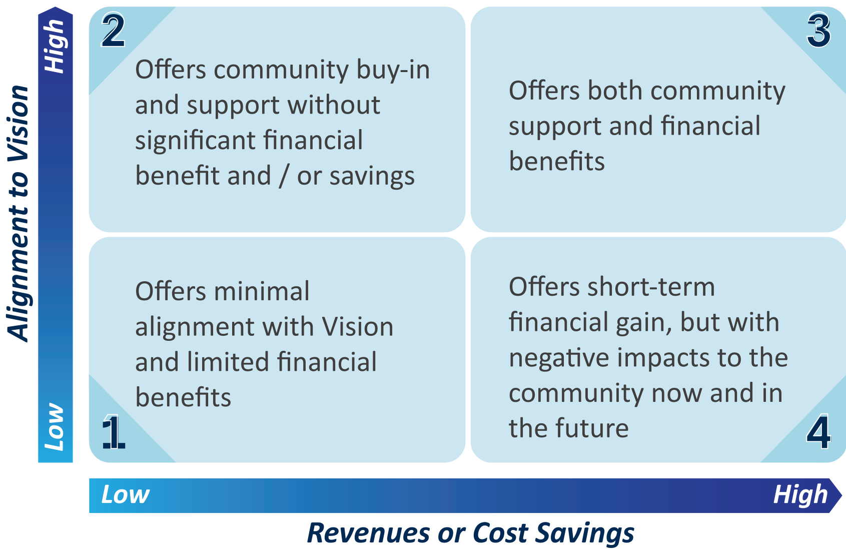
These exercises look into the current state of the utility, case studies from initiatives taken by others not necessarily only in Ontario, and identifying potential solutions based on the information gathered and non-traditional thinking.

There are a number of directions LDCs could go, but here are a few options worth considering.

Option One – **Maximize the Relationship Between the Utility and the Municipality.**

You already have an established relationship with your municipality, and in most instances, your principal shareholder; why not look for ways on how you can make it stronger? Utilities can provide very strong annual revenues and dividends to a municipality each year, and developing a more strategic partnership between the two entities can benefit both handsomely.

In order to maximize this relationship, the utility would need to align their potential revenues or cost savings with the vision of the municipality. The following graph outlines the relationship between vision and revenues or cost savings.



The first quadrant is an area which should be avoided since there is low alignment to the vision and low return on revenues or cost savings. This might include introducing a usage fee for public facilities. However, the third quadrant signifies both a strong alignment to the vision and a high return on revenues or cost savings.

This is where initiatives such as job creation are implemented to benefit both the municipality and the utility. Special attention should be paid to this quadrant when researching future options.

Option Two –
It's all About Having a Plan – Actively Manage Your Asset Base.

LDCs should consider developing a program where asset management is an ongoing activity with small, achievable goals each year.
By leveraging this type of program, utilities are able to make better informed decisions rather than making short-term financial and technical decisions in an effort to curb the trend or ignore the deterioration.

Setting aside sufficient funds to operate, maintain, and replace assets will maintain public confidence, protect community values and goals, and help drive economic development.

Option Three –
Leverage Your Strengths.

There are a number of things that you are already doing well today. One avenue to explore is taking those strengths and leveraging them elsewhere.
For example, LDCs could create an affiliate company that could take on a shared services mandate. This would include managing infrastructure maintenance, billing, a customer care centre, as well as water and wastewater services. If a utility were to partner with the municipality, the affiliate company could manage services such as property taxes, solid waste and other asset management services.
Expenses, such as benefits and payroll services could also be consolidated, resulting in more cost savings opportunities.

The Bottom Line

The market is rife with uncertainty, but LDCs must start to create innovative methods to ensure future success.
There are initiatives you can participate in now that will satisfy your stakeholders and the public.
Investing the time now to research, identify and develop a series of feasible options will give LDCs the confidence to make informed decisions in the future, ensuring that careful consideration is taken to include stakeholders, achieving public buy-in, and maintaining transparency.

Engaging in a future options exercise today will ensure LDCs have carefully researched, fact-based evidence to make informed decisions regarding their business – and you don't need to pull out the dynamite to get there.

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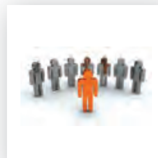

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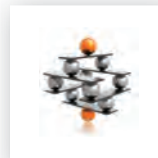

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