



**BY EMAIL and RESS**

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December 18, 2017  
Our File: EB20170056

**Attn: Kirsten Walli, Board Secretary**

Dear Ms. Walli:

**Re: EB-2017-0056 – Kitchener-Wilmot Hydro Inc. 2018 – SEC Submissions**

We are counsel to the School Energy Coalition (“SEC”). Pursuant to Procedural Order No. 1, these are SEC’s submissions on the request by Kitchener-Wilmot Hydro Inc. (“KWHI”) to correct errors in balances in two Retail Settlement Variance Accounts (“RSVA”) that were previously approved and cleared on a final basis by the Board.

SEC submits that the Board should require KWHI to refund amounts that were overcharged due to its errors that led to the Board approving rates that were not based on correct amounts. At the same time, it should not require customers to offset those credits, by requiring those who may have been undercharged by the errors, to now pay. The application of retroactive ratemaking to circumstances such as these is not symmetrical.

### **Overview**

In KWHI’s 2016 IRM rates application (EB-2015-0084), after questions were raised by Board Staff, it was revealed that due to a manual record error, there were significant misallocations of amounts in RSVA Accounts 1588 (Power) and 1589 (Global Adjustment). This included amounts up to the end of 2013 that had been cleared a year earlier on a final basis in KWHI’s 2015 IRM rates application (EB-2014-0089).<sup>1</sup> KWHI sought to correct the errors as well as clear its more recent balances but the Board, by way of delegated authority, denied its request. The Board did not allow KWHI to correct the errors as it “raise[d] questions of retroactive ratemaking that go beyond the scope of th[e] proceeding”.<sup>2</sup> The Board also determined that due to irregularities found, it would not approve the disposition of balances in Accounts 1588 and 1589 until its Audit and Performance Assessment unit conducted a regulatory audit.<sup>3</sup>

Since the 2016 IRM proceeding, KWHI determined that there were two additional errors which led to further incorrect balances in Accounts 1588 and 1589.

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<sup>1</sup> Audit of Kitchener-Wilmot Hydro Inc.’s Selected Deferral and Variance Accounts and RPP Settlement, April 7 2017 (Appendix A to Interrogatory Responses)

<sup>2</sup> *Decision and Rate Order* (KWHI – 2016 IRM), December 10 2015, p.7

<sup>3</sup> *Ibid*

The three errors include:

- a. **Error 1.** A senior regulatory analyst manually entered an incorrect amount into a worksheet which was not detected by the responsible manager “due to pressures that included preparing for an Oral Hearing”.<sup>4</sup>
- b. **Error 2.** Monthly adjustments to accrue for unbilled revenue did not separate power expenses into GA and Power components until December 2014. This occurred even though the billing system was adjusted to split the Power and GA amounts as of October 2013, but KWHI’s accrual spreadsheets were not updated until December 2014.<sup>5</sup> This led to balances being allocated to the wrong accounts. This error had the largest impact.<sup>6</sup>
- c. **Error 3.** Instead of using the actual IESO bill to record the GA variance, KWHI used the Final Settlement amount.<sup>7</sup> This error was immaterial.<sup>8</sup>

KWHI is now seeking to make adjustments to correct all three errors. The effect of the errors is that due to the misallocation of balances in these accounts, certain customers were overcharged and others were undercharged in 2015, for 2013 balances. Since account 1589 is paid by non-RPP customers who are charged the Global Adjustment through this account, the effect was primarily overpayment by GS>50 customers which include many schools.<sup>9</sup> KWHI’s proposal would result in amounts being charged to certain customers who were undercharged due to its errors, and credits to those who were overcharged.<sup>10</sup>

### ***Retroactive Ratemaking***

Since there is no dispute that the 2013 balances have been cleared on a final basis, the Board must determine if the correction proposed by KWHI constitutes prohibited retroactive ratemaking. If it is, then the Board is legally prohibited from making such an adjustment. If it is not, then the Board still must determine if it should exercise its discretion to order the adjustment.

In doing so, it is important for the Board to determine the question separately for undercharged parties and overcharged parties. This is because the rule against retroactive ratemaking is not strictly symmetrical. While the Board is prohibited from collecting, through future rates, additional amounts that should have been included in past rates, the converse is not true. Refund to ratepayers of amounts that should have not been included in past approved rates has been allowed in many cases.

In the case where past rates were too low, there is a clear rule. The well-established rule against retroactive ratemaking is that the Board can only act prospectively in setting rates. That means the

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<sup>4</sup> Pre-Filed Evidence p.11; SEC-3

<sup>5</sup> *Ibid*

<sup>6</sup> Pre-Filed Evidence p.12, Table 4

<sup>7</sup> Pre-Filed Evidence p.12; SEC-3

<sup>8</sup> Pre-Filed Evidence p.12

<sup>9</sup> Pre-Filed Evidence p.13-14. SEC notes that Class A GS>50 customers are not charged Global Adjustment through Account 1589 as they settle directly with their utility based on Industrial Conservation Initiative.

<sup>10</sup> In response to Staff-13, KWHI provided bill impacts with and without the proposed adjustments that show all customer classes better off. There is clearly an error in this calculation as the entire proposal is to credit some customers will require others to pay offsetting additional amounts. It does not make sense that all customers benefit from the adjustment.

Board may not establish rates that recover expenses or costs incurred in the past, and were not recovered through the final rates established for those past periods.<sup>11</sup>

One key principle behind the rule is that rates are presumed to be final, and are just and reasonable until altered. As the Board has previously stated, “the principles of certainty and finality are a necessary component of effective rate regulation.”<sup>12</sup> Consumers make consumption decisions based on the price of electricity at any given time, and a utility similarly makes business decisions based on the revenue they expect to receive through those same rates.

Further, intergenerational equity concerns exist for consumers, as yesterday’s customers may not be today’s customers. To be able to adjust future rates for past costs has been held to be “most unreasonable”.<sup>13</sup>

The rule against retroactive ratemaking is not a discretionary decision by the Board; if it is found to be applicable, it prevents the adjustment from being made unless there is a recognized exception<sup>14</sup> to the rule.<sup>15</sup> The generally accepted exceptions are a) rates are interim, or b) a deferral or variance account “encumbers” past amounts with the expectation of all parties that they will be adjusted in the future.<sup>16</sup> Neither of these exceptions is available for the amounts at issue in this proceeding. The amounts for the period up until the end of 2013 in those accounts were cleared for those years on a final basis in 2015.

The analysis is different when it comes to refunds to overcharged customers. The Board has in the past concluded that it has authority to order *credits* going forward for a one-time adjustment to a past overpayment of costs that the regulator finds unjust, and that does not constitute retroactive ratemaking.<sup>17</sup> As noted previously by Vice Chair Kaiser in dissent (on the issue of whether retroactive ratemaking was engaged on the facts, not its scope):

There is ample authority in the regulatory jurisprudence that credits going forward do not constitute retroactive ratemaking”. This is particularly the case where it reflects a one-time fixed amount adjustment to an overpayment that the tribunal finds unjust.<sup>18</sup>

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<sup>11</sup> *Union Gas Limited v. Ontario Energy Board*, 2015 ONCA 453, para 82; *Decision and Order* (RP-2005-0013/EB-2005-0031 - Great Lakes Power), February 24, 2006, p.17, citing *Northwest Utilities Ltd. v. City of Edmonton*, [1979], 1 S.C.R. 684. *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] 1 S.C.R. 140, para 71

<sup>12</sup> *Decision and Rate Order*, (EB-2013-0119 – Chapeau PUC) March 13 2014, p.8; *EB-2013-0022, and Order* (EB-2013-0022 – Veridian), April 25, 2013, p.10

<sup>13</sup> *R. v. Board of Public Utilities Commissioners* (1966), 60 D.L.R. (2d) 703, para 25.

<sup>14</sup> There is confusion in the language in many decisions on retroactive ratemaking. Some consider certain situations where the rule does not apply as exceptions, others treat them as simply contours that define its general scope. See for example, *Northland Utilities et al v. NWT Public Utilities Board*, 2010 NWTSC 92, para 5, regarding the exception for deferral accounts, compared to *Bell Canada v. Bell Aliant Regional Communications*, [2009] SCC 40 the leading authority on the issue, in which the Supreme Court makes no reference to it being an exception. Further, see the discussion in *Calgary (City) v. Alberta (Energy and Utilities Board)*, 2010 ABCA 132 beginning at para. 163.

<sup>15</sup> *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, 2006 SCC 4 [“ATCO SCC 2006”], para 71; *Decision and Order* (EB-2005-0031 - Great Lakes Power), February 24 2006, p.8.

<sup>16</sup> *Bell Canada v. Canada (Canadian Radio Television and Telecommunications Commission)*, [1989] 1 S.C.R. 1722; *Bell Canada v. Bell Aliant Regional Communications*, [2009] 2 S.C.R. 764

<sup>17</sup> *Decision and Order* (EB-2014-0043 – Enbridge), April 10 2014; *Decision and Order* (EB-2005-0031 - Great Lakes Power), February 24 2006, p.17

<sup>18</sup> *Decision and Order* (EB-2005-0031 – Great Lakes Power), February 24 2006, p.21, citing *New York Water Service Corp v. Public Service Commission*, 208 N.Y.S. 2d 587 (1960) see *ATCO SCC 2006*, para. 137

This should not come as much of a surprise, since utilities have a significant asymmetry of information over ratepayers and the Board. They should not be allowed to benefit from their mistakes, which only they have the ability to reveal.

The overarching principle is the knowledge of the utility and consumers that rates may change retrospectively.<sup>19</sup> The Alberta Court of Appeal has summarized what is the essential inquiry in determining if a ratemaking decision that impacts on past rates is impermissible: “the critical factor for determining whether the regulator is engaged in retroactive ratemaking is the parties’ knowledge.”<sup>20</sup>

Consistent with the principle behind those exceptions to the rule, a utility knows that if they make accounting or similar errors in limited circumstances which results in customers overpaying, then the Board has the discretion to order it to repay the overcharge.<sup>21</sup> This is because they control their books. In a similar situation of misallocation of costs between accounts 1588 and 1589, the Board discussed the harms of these errors on customers and the range of options available to the Board:

Utilities such as Essex Powerlines have ultimate control of their books and records and therefore bear the responsibility of ensuring that there are no mistakes in their filings with the Board. Errors crystalized in final rates can have long term adverse impacts on consumers. In situations where errors are the result of a utility’s negligence, the Board could impose financial or other consequences on the utility. For example, the Board could order the utility to repay customers, deny the accrual of interest on outstanding balances or deny the inflation adjustment to base rates.<sup>22</sup>

There is no requirement for symmetrical treatment in situations of retroactive ratemaking. In that same decision, the Board found that innocent third party customers can be treated differently than that of the utility:

Does the rule against retroactive ratemaking prohibit the refund of money to customers because rates were declared final? RPP customers are innocent third parties. There is Board precedent for requiring a utility to repay money to customers if negligent or if the utility would profit on account of its own errors (EB-2009-0013 and EB-2014-0043). In other words, the Board is not driven by a need for symmetrical treatment of customers and utilities in final rate situations.<sup>23</sup> [emphasis added]

In the decisions cited by KWHI regarding adjustments to previous DVA balances cleared on a final basis, all that do involve a question of retroactive ratemaking, are situations where the Board has only allowed refunds of out-of-period adjustments to customers.<sup>24</sup> This includes, most recently, the Board’s decision in EB-2016-0090, where Lakeland Power Distribution was allowed to make adjustments to previously cleared amounts since it resulted in a refund to customers. In that

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<sup>19</sup> *Bell 2*, para. 61

<sup>20</sup> *ATCO 2014*, para 58. See also *Milner Power Inc. Complaints regarding the ISO Transmission Loss Factor Rule and Loss Factor Methodology ATCO Power Ltd.* (Alberta Utilities Commission, Proceeding 790), January 20 2015, para. 194-195

<sup>21</sup> *Decision and Order* (EB-2014-0043 - Enbridge), April 10 2014; *Decision and Order* (EB-2009-0113 – North Bay Hydro), September 8, 2009, p.10; *Decision and Order* (EB-2005-0031 - Great Lakes Power), February 24 2006, p.17

<sup>22</sup> *Partial Decision and Procedural Order No.3* (EB-2014-301/0072 -- Essex Powerlines), March 25 2015, p.7

<sup>23</sup> *Ibid*

<sup>24</sup> Staff-14. SEC notes that KWHI cited EB-2016-0066 (E.L.K. Energy). In that matter there was never an issue of retroactive ratemaking. The issue in that proceeding was that ELK due to an error had not actually billed certain customers an approved and correct rate rider for certain DVAs. Because of that the unbilled amounts were recorded in account 1595, which acts as a residual account to ensure approved and cleared amounts are collected.

decision, the Board repeated that there is no need for symmetrical treatment between ratepayers and utilities where the basis of the error is the utility's mistakes.<sup>25</sup>

***Over-collected Amounts Should Be Returned and KWHI Should Be Responsible For Its Errors***

SEC submits KWHI's procedures and oversight were clearly inadequate. The over-collected amounts should be refunded. Those customers should not be penalized because of KWHI's mismanagement. They have overpaid for their electricity consumption, based on rates that were declared final, between January 1<sup>st</sup>, 2015 and December 31<sup>st</sup>, 2015.<sup>26</sup> The Board should exercise its discretion and order KWHI to credit those customers who, due to the errors, have overpaid. Based on KWHI evidence, it has overcharged non-RPP customers who pay amounts in 1589 by \$2,195,104.<sup>27</sup>

At the same time, the Board should not require customers who have underpaid the equivalent aggregate amount, due to the errors in Account 1588, to have to now pay.<sup>28</sup> To do so would be impermissible retroactive ratemaking.

SEC submits it is fair that KWHI should be responsible for the \$2,195,104 that due to its errors, non-RPP customers overpaid. In 2015, the year the riders clearing the 2013 balances on a final basis were charged, it over-earned and achieved an ROE of 11.47%. Based on its forecast 2018 budget, if KWHI's shareholder was required to pay for the overcharged amount, it would only result in a reduction of forecast ROE by 2.32%.<sup>29</sup> If the Board submits the annual amount would be too great, it could require a refund rider of the Account 1589 overcharge over a 2 year period.

While it is true that the distributor overcharge was not intentional, it still resulted in certain customers being required to pay through rates more than they should have due to KWHI's errors. This is not about intent. It is about responsibility.

A regulated monopoly distributor such as KWHI must have accounting systems, both regulatory and financial, that have checks and balances built in to prevent errors from happening. This is especially important when calculations and entries are made manually. KWHI provided no evidence that any processes were in place to ensure the senior regulatory analyst was double and triple checking the calculations and entries. The oversight provided by the manager was clearly inadequate. As KWHI admits, the responsible manager did not catch the issue because he or she was preoccupied with the pressures of other matters. This is a troubling admission. While SEC recognizes that regulatory proceedings are stressful for those involved, it cannot be a valid excuse for individuals to perform their day to day responsibilities negligently.

The second error, which had the greatest impact, may even be more concerning. KWHI's evidence is that even though it programmed its CIS system by October 2013 to split out the unbilled revenue between Power and Global Adjustment, its spreadsheet did not account for the split until December 2014.<sup>30</sup> This was after its 2015 rates application was filed and considered by the Board.<sup>31</sup> No

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<sup>25</sup> *Decision and Order* (EB-2016-0090 - Lakeland Power Distribution Ltd), December 8 2016, p.9

<sup>26</sup> The Rate Riders approved were in place between January 1 2015 and December 31 2015 as set out in the various approved tariffs. See *Decision and Rate Order* (EB-2014-0089 -- KWHI), December 4 2014, Corrected December 19 2014

<sup>27</sup> Pre-Filed Evidence p.12, Table 4

<sup>28</sup> SEC-5

<sup>29</sup> SEC-5; Forecast 2018 ROE (\$6,727,477 represents an ROE of 7.10%, which equals a 1% increase in ROE is equivalent to \$947,532).  $\$2,195,104/\$947,532 = 2.32$

<sup>30</sup> SEC-3

<sup>31</sup> The Board issued its Decision and Rate Order in EB-2014-0089 on December 4, 2014. It later issued correction due to a typographical error related to the wording on the tariff on December 19, 2014.



rationale has been provided to explain why KWHI's spreadsheet was not updated until December 2014, when the requirement to separate the amounts had been in place since the beginning of 2012<sup>32</sup>, and its computer system was able to do so automatically since October 2013.

Further, the evidence is that KWHI knew of this error in 2014.<sup>33</sup> This presumably was around the time it finally corrected its spreadsheet, yet did not bring it to the Board's attention right away and did not bring a motion to review. If it had, it would have likely been within the time frame allowed under the Board's Rules. Further, in its 2016 rate case, while there is discussion of Error #1, KWHI does not appear to have raised the issue of Error #2. This is very troubling.

As of today, KWHI still does not have documented procedures for internal monitoring of these accounting processes.<sup>34</sup>

**Conclusion**

The evidence in this proceeding demonstrates that KWHI was clearly negligent in its regulatory accounting that led to the errors, and it should bear the cost of refunding to customers amounts overcharged due to its own errors in the calculation of Account 1589.

Yours very truly,  
**Shepherd Rubenstein P.C.**

*Original signed by*

Mark Rubenstein

cc: Wayne McNally, SEC (by email)  
Applicant and Interested parties (by email)

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<sup>32</sup> SEC-3

<sup>33</sup> VECC-2(e)

<sup>34</sup> VECC-2(a)(iii)