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BY E-MAIL

July 4, 2018

Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: Essex Powerlines Corporation (Essex Powerlines)
2018 Distribution Rate Application
OEB Staff Submission
OEB File No. EB-2017-0039

In accordance with Procedural Order No. 4, please find attached OEB staff's submission on the unsettled issue for Essex Powerlines' 2018 cost of service application. This document is also being forwarded to Essex Powerlines, the School Energy Coalition, the Vulnerable Energy Consumers Coalition, and Hydro One Networks Inc.

Yours truly,

Original Signed By

Donald Lau
Project Advisor – Rates Major Applications

Encl.

2018 ELECTRICITY DISTRIBUTION RATES

Essex Powerlines Corporation

EB-2017-0039

OEB STAFF SUBMISSION

July 4, 2018

INTRODUCTION

On April 13, 2018, Essex Powerlines Corporation (Essex Powerlines) filed a settlement proposal in the current proceeding in which the parties (Essex Powerlines and the intervenors, which included Hydro One Networks Inc. with respect only to the proposed Embedded Distributor Rate; School Energy Coalition (SEC); and Vulnerable Energy Consumers Coalition (VECC)), reached complete settlement with the exception of an issue related to the Group 1 DVA balances as at December 31, 2013, which were approved on an interim basis in the 2015 IRM Decision and Order, for a net recovery amount of $1.8 million from customers as identified in an Ontario Energy Board (OEB) audit.

As discussed below, this matter has a history that dates back to Essex Powerlines' 2012 incentive rate-setting mechanism (IRM) application, in which Essex Powerlines sought approval for the disposition of balances in various Deferral and Variance Accounts (DVAs). More particularly, the matter relates not only to the current proceeding, but also has its origins in the following Essex Powerlines rate adjustment applications:

- 2012 IRM proceeding
- 2014 IRM proceeding
- 2015 IRM proceeding[1]

As ordered in Procedural Order No. 2, Essex Powerlines filed additional information pertaining to the unsettled issue on May 17, 2018. OEB staff and intervenors filed interrogatories on May 24, 2018 and Essex Powerlines responded on June 7, 2018. The parties to the settlement proposal (specifically, Essex Powerlines, SEC and VECC, as Hydro One's involvement was limited to the Embedded Distributor rate) proposed that the unsettled issue be resolved through written submissions. The OEB, in its Procedural Order No 4, accepted the parties' proposed process starting with Essex Powerlines' argument-in-chief, followed by submission from OEB staff and intervenors, and reply submissions from Essex Powerlines.

[1] EB-2011-0166, EB-2013-0128, EB-2014-0072

OEB staff's submissions are set out below. In short, OEB staff submits that the OEB should approve, on a final basis, the Group 1 DVA balances as at December 31, 2013, which were approved on an interim basis in the 2015 IRM Decision and Order.[2]

[2] EB-2014-0072, Decision and Order, June 9, 2015

BACKGROUND

In its June 9, 2015 decision on Essex Powerlines' 2015 IRM application[3], the OEB ordered that a complete audit be undertaken of all DVAs (except Accounts 1555 and 1556), and of the accounting procedures and controls that Essex Powerlines has in place. This was to ensure all DVA entries and balances were accurate for 2013 and on a going forward basis. The OEB approved the disposition of Group 1 DVA balances as at December 31, 2013, on an interim basis

The OEB's Audit and Performance Assessment department (Audit Department) completed its audit report on the balances of Essex Powerlines' Group 1 and Group 2 DVAs on March 21, 2017 (Group 1 & 2 Audit). Essex Powerlines agreed with all of the findings and observations outlined in the Group 1 & 2 Audit, with the exception of Finding 10.1 (discussed below) and consequently did not make the adjustments to the DVA balances recommended by OEB staff in that particular finding. Essex Powerlines has made all other adjustments recommended by OEB staff, consistent with the Group 1 & 2 Audit.

Finding 10.1 addresses an adjustment that Essex Powerlines made to DVA balances as part of its 2015 IRM proceeding that had previously been approved for disposition on a final basis. The adjustment had also not been specifically identified in its 2015 IRM application. Essex Powerlines made this adjustment because, as a result of accounting errors made by Essex Powerlines, a refund was credited to customers twice – first, in Essex Powerlines' 2012 IRM proceeding[4]; and again in Essex Powerlines' 2014 IRM proceeding.[5]

The DVA balances in question related to activities to the end of December 31, 2010. The adjustment consisted of a journal entry made on December 31, 2014 to transfer the 2010 amounts (that were reviewed originally in the 2012 IRM application) to Account 1595. This adjustment was made because Essex Powerlines failed to make this transfer originally following the approved disposition of the 2010 balances in the 2012 IRM decision. Because Essex

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[3] EB-2014-0072
[4] EB-2011-0166
[5] EB-2013-0128

Powerlines failed to make the transfer to the 1595 tracking account at the required time, the 2010 balances remained in the main control accounts and were disposed a second time as part of the 2014 IRM proceeding. Essex Powerlines made the adjustment as part of its 2015 IRM proceeding in order to reverse the duplicate refund that had occurred. By making this adjustment, it enabled recovery from its customers of an amount roughly equal to $1.8 million. The OEB allowed this correction to be implemented on an interim basis as part of the 2015 IRM decision, pending the review by the OEB's Audit Department. A detailed explanation of the balances can be found in the Chronology of Events section below.

In its Group 1 & 2 Audit report, the OEB Audit Department's view was that the adjustment in question should not be reflected in the Essex Powerlines DVA balances as of December 31, 2015. The OEB Audit Department noted that the filing requirements for 2015 rate applications state that the OEB expects that no adjustments should be made to any DVA balances previously approved by the OEB on a final basis.[6] The adjustment made on December 31, 2014 would be adjusting balances that had already been disposed on a final basis in a prior proceeding.

The filing requirements further state that if in fact a distributor has made adjustments it must provide an explanation in the application for the nature of the adjustments.

Essex Powerlines acknowledged in this current proceeding that this adjustment was not explained in the manner set out in the filing requirements but pointed out that the adjustment was addressed in the 2015 IRM proceeding through submissions.[7]

Unsettled Issue

The unresolved issue pertains to the interim recovery by Essex Powerlines of the erroneous duplicate credit of $1.8 million from customers identified in finding 10.1

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[6] Filing Requirements for 2015 Electricity Distribution Rate Applications, Chapter 3, page 9, issued July 25, 2014

[7] EB-2014-0072 - Essex_ReplySub_Final EPL response_011915_20150119, January 19, 2015

of the Group 1 & 2 Audit report.[8] Essex Powerlines has proposed to finalize this interim recovery in the current proceeding. To assist the OEB, OEB staff offers additional analysis of this issue below. The further discovery process afforded for this issue in the current proceeding has provided OEB staff with a better understanding of the course of events which has led to OEB staff's conclusion that the adjustment made by Essex Powerlines in the 2015 IRM proceeding should be accepted and finalized as proposed by Essex Powerlines.

[8] EB-2017-0039 Essex Powerlines Interrogatory Response, March 2, 2018 (9-Staff-80b)

Chronology of events:

A. 2012 IRM proceeding EB-2011-0166:

In Essex Powerlines' 2012 IRM proceeding the OEB approved the disposition (on a final basis) of DVA balances with a net credit totaling $3,551,660, per Table 1 below.

Table 1: Approved disposition of balances as of December 31, 2010

Account Name	Account Number	Total including Interest
LV Variance Account	1550	-$20,649
RSVA – WMSC	1580	-$998,288
RSVA – Retail Transmission Network Charge	1584	$1,188,240
RSVA – Retail Transmission Connection Charge	1586	-$333,885
RSVA – Power (excluding GA)	1588	$1,640,471
RSVA – Power Sub-Account Global Adjustment	1588 GA	-$3,310,147
Recovery of Regulatory Asset Balances	1590	-$1,618,215
Special Purpose Charge variance	1521	$10,738
PILs Deferred Payments in Lieu of Taxes	1562	-$109,924
Total approved per Decision		-$3,551,660

In the decision that approved the DVA account balances for disposition, the OEB ordered that:

> The respective balance of each Group 1 Account approved for disposition shall be transferred to the applicable principal and interest carrying charge sub-accounts of Account 1595 pursuant to the requirements specified in Article 220, Account Descriptions, of the *Accounting Procedures Handbook for Electricity Distributors*. The date of the journal entry to transfer the approved account balances to the sub-accounts of Account 1595 is the date on which

> disposition of the balances is effective in rates, which generally is the start of the rate year (e.g. May 1).'[9]

The transferred balance in Account 1595 subaccount (2012) would then be drawn down through the implementation of the approved rate riders. In the future, subsequent to the sunset date of the rate riders, and once all transactions relating to Account 1595 subaccount (2012) were completed, Essex Powerlines would come forward in a future rate application and seek disposition of the audited residual balance of this sub-account. In this case Essex Powerlines neglected to transfer the amounts from the DVA accounts to Account 1595 subaccount (2012).

The impact of this oversight was that the amounts from the implemented rate riders that were charged to or refunded to customers (and that were tracked in account 1595 subaccount (2012)), did not draw down any approved balances because there were no approved balances residing in Account 1595. As a result, Essex Powerlines has shown in its interrogatory response that Account 1595 subaccount (2012) accumulated $1,873,162 between 2012 and 2014 (the time period when the approved rate riders were in effect).[10]

Moreover, since Essex Powerlines failed to transfer the Group 1 DVA account balances to account 1595 (2012) the following amounts, set out in Table 2 below, totaling a net amount of approximately $1.8 million, remained in the Group 1 main control DVA accounts, and were subsequently disposed of a second time in Essex Powerlines' 2014 IRM application:

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[9] EB-2011-0166, Decision and Order, April 4, 2012

[10] Essex Powerlines Interrogatory Responses – Procedural Order #2, June 7, 2018 (IR2-Staff-2)

Table 2: DVA Account Balances Disposed Twice

Account Name	Account Number	Total including Interest
LV Variance Account	1550	-$20,649
RSVA – WMSC	1580	-$998,288
RSVA – Retail Transmission Network Charge	1584	$1,188,240
RSVA - Retail Transmission Connection Charge	1586	-$333,885
RSVA – Power (excluding GA)	1588	$1,640,471
RSVA – Power Sub-Account Global Adjustment	1588 GA	-$3,310,147
Total		**-$1,834,258**

Account 1595 (2012) has not to date been disposed of on a final basis, however it was disposed of on an interim basis in the 2015 IRM proceeding. OEB staff notes that no DVA disposition took place as part of the 2013 IRM proceeding (in which the balances reviewed were as of year-end 2011).

B. 2014 IRM proceeding EB-2013-0128:

In Essex Powerlines' 2014 IRM proceeding, Essex Powerlines requested that the OEB approve the disposition (on a final basis) of the December 31, 2012 balances in its DVA accounts with a net credit balance of $4,592,942, as set out in Table 3 below.

Table 3: Approved disposition of balances as of December 31, 2012

Account Name	Account Number	Total disposed including Interest
LV Variance Account	1550	$727,886
RSVA – WMSC	1580	-$3,720,954
RSVA – Retail Transmission Network Charge	1584	$378,816
RSVA - Retail Transmission Connection Charge	1586	-$1,312,577
RSVA – Power	1588	$9,603,667
RSVA – Global Adjustment	1589	-$8,786,415

Recovery of Regulatory Asset Balances	1590	-$1,483,365
Total per Decision		-$4,592,942

As noted above, these balances included the approved year end 2010 amounts from the 2012 IRM proceeding that are shown in Table 2 as having been disposed of twice. The OEB granted the requested approval, and Essex Powerlines transferred the Group 1 DVA balances as at December 31, 2012 to Account 1595 subaccount (2014) on May 1, 2014 as directed by the OEB in its 2014 IRM decision.

However, since Essex Powerlines had not transferred the Group 1 DVA balances as at December 31, 2010 to account 1595 (2012) following the 2012 IRM proceeding, those December 31, 2010 Group 1 DVA balances were carried forward to the December 31, 2012 Group 1 DVA balances and include in the calculation of the rate riders with the result that the December 31, 2010 balances were disposed of a second time, returning an additional $1,834,258 to customers as shown in Table 2 above.

Essex Powerlines has not to date applied for the disposition of the residual balance in account 1595 (2014).

C. 2015 IRM proceeding EB-2014-0072:

In Essex Powerlines’ 2015 IRM proceeding the OEB approved the disposition (on an interim basis) of DVA accounts with a net credit balance of $2,060,341, per Table 4 below.

Table 4: Approved disposition of balances as of December 31, 2013[11]

Account Name	Account Number	Total including Interest and correction of duplicate disposition
LV Variance Account	1550	$643,592
Smart Metering Entity variance	1551	$47,653
RSVA – WMSC	1580	$234,955
RSVA – Retail Transmission Network Charge	1584	-$1,405,299
RSVA - Retail Transmission Connection Charge	1586	-$1,023,940
RSVA – Power	1588	-$2,151,441
RSVA – Global Adjustment	1589	$3,293,417
Recovery of Regulatory Asset Balances	1590	-$1,510,347
Recovery of Regulatory Asset Balances	1595 – 2012	-$188,931
Total Disposition		**-$2,060,341**

The balances in Table 4 above reflect an adjustment to the DVA Continuity Schedule in the 2015 IRM Rate Generator Model that reversed the duplicated amounts in Table 2 above to correct for the duplicate refund relating to the $1,834,258 from the 2014 IRM rate application. The adjustment was made to the opening Group 1 DVA balances as at January 1, 2013 and a similar adjustment was made to Account 1595 subaccount (2012) account so that the 2012 sub account would now reflect a drawdown of the originally approved balances. Because the revenues or credits realized through the rate riders will vary based on consumption, there is now a residual debit balance in account 1595 (2012) of $195,923.

Essex Powerlines transferred the DVA balances as at December 31, 2013 to Account 1595 subaccount (2015) on May 1, 2015 as directed by the OEB in the 2015 IRM decision.

[11] OEB staff used the evidence filed under IR2-Staff-2 a), Attachment 1-B to create the above Table, as the Decision and Order EB-2014-0072 was in another format as it dealt with the issues that were before the OEB in that proceeding.

Essex Powerlines has not to date proposed disposition of the residual balance in Account 1595 (2015).

OEB Staff Submission:

OEB staff agrees with the Audit Department that the adjustments were initially made without adequate disclosure in the 2015 IRM proceeding and that Essex Powerlines' DVA continuity schedule filed with its 2015 IRM rate application did not agree with its accounting records.

As noted earlier, once DVA account balances are approved for disposition, the utility should move the DVA amounts from each individual DVA into the appropriate subaccount of Account 1595 for the relevant rate application year. If the net DVA account balances approved are debits (i.e. collectible from ratepayers), then the total amount moved into the appropriate subaccount of Account 1595 would be a debit. As the utility collects the revenue from the rate riders, the account balance would be drawn down. After the sunset date of the rate riders and all recovery transactions have been recorded, the utility would propose the disposition, in the next rate application, of the residual balance of the subaccount of Account 1595.

This is the second proceeding in recent years in which the OEB is faced with a major accounting error by Essex Powerlines related to DVAs. In the 2015 IRM proceeding, the OEB was faced with a series of errors that Essex Powerlines made to DVA balances spanning 2011 through 2013. The audit that is the subject of this current application arose from those errors. In that proceeding, the OEB noted the following[12]:

> Unfortunately this proceeding devolved, in large part, into a forensic accounting exercise in which the OEB found it necessary to ask two sets of supplemental questions through procedural orders, in order to understand the evidence and clarify the record. Moreover, considerable resources were required by the OEB and the parties

[12] EB-2014-0072, Decision and Order, June 9, 2015

> to decipher the three sets of continuity schedules filed after the interrogatory phase of the proceeding.

The OEB also found that, "…based on the evidentiary record, Essex Powerlines demonstrated carelessness towards ensuring proper regulatory accounting procedures and controls."

As a consequence of the accounting errors made to the 2011-2013 balances, the OEB denied the aspect of the application made by Essex Powerlines for a base rate increase based on the Price Cap IR formula. The increase would have generated approximately $160,000 in additional revenue.

OEB staff submits that Essex Powerlines has once again demonstrated a lack of care with its accounting records. In this instance however, due to the nature of Account 1595 and the fact that residual balances in the relevant Account 1595 subaccounts have not been disposed of on a final basis, OEB staff submits that the adjustment made in the 2015 IRM proceeding should be approved. Although the approach Essex Powerlines took (i.e. making adjustments to the DVA continuity schedule for the amounts provided in Table 2 above) is not consistent with the filing requirements, the end result was the same (i.e. to draw down the originally approved balance in Account 1595 (2012)). This is consistent with the nature and purpose of Account 1595.

Moreover, since Essex Powerlines would still be able to request disposition of the residual amount in Account 1595 subaccount (2012) had it not made this adjustment, and since Account 1595 subaccount (2012) reflected the full implementation of the approved rate riders from the 2012 IRM proceeding (with no draw down of the originally approved amounts), the end result would have been the same (i.e. disposition of the balance of Account 1595 subaccount (2012)). OEB staff notes that Account 1595 subaccount (2012) had not been approved for disposition on a final basis.

In its argument-in-chief, Essex argues that the correction of an error does not represent retroactive rate making.[13] OEB staff submits that since the issue in this case relates to the balances in subaccounts of Account 1595, and as there have

[13] Essex Powerlines argument-in-chief, June 22, 2018, at pages 3-6.

been no OEB orders that dispose of the residual balances in those subaccounts on a final basis, whether for 2012, 2014 or 2015, there is no issue of retroactive ratemaking in this case.

OEB staff submits that if the OEB approves Essex Powerlines' proposal to finalize the interim dispositions, the rate payers as well as the utility would be held whole, and OEB staff agrees that those interim dispositions should be finalized. However, it is important to note that Essex Powerlines erred in duplicating the disposition of the amounts set out in Table 2, from May 1, 2014 to April 30, 2016. This resulted in additional debits accumulating in Account 1595 (2014) relating to the duplication, and Essex Powerlines accrued carrying charges on the debits which accumulated in Account 1595 (2014).

OEB staff submits that Essex Powerlines should not be permitted to recover the additional carrying charges recorded in Account 1595 (2014) related to the duplicate disposition, in the approximate amount of $22,000, as allowing the recovery of those carrying charges would effectively enable Essex Utilities to profit from its own error. OEB staff submits that Essex Powerlines should provide a calculation of the carrying charges that would have accrued on the double disposed net amount of $1.8 million and credit the balance in Account 1595 (2014) by that amount for calculating the draft rate order.

OEB staff notes that the OEB has conducted a follow up audit to determine the status of Essex Powerlines' accounting controls and processes. OEB staff submits that in its next rate application, Essex Powerlines should be required to file a report detailing its implementation of the OEB Audit Department's recommendations and any other improvements that Essex Powerlines has implemented to prevent more accounting errors from occurring in the future.

All of which is respectfully submitted