EB-2008-0205

THE ONTARIO ENERGY BOARD

IN THE MATTER OF the Ontario Energy Board Act, 1998, S.O. 1998, c. 15, (Schedule B);

AND IN THE MATTER OF an application by Oshawa PUC Networks Inc. for an order or orders approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2009.

SUBMISSIONS

OF THE

SCHOOL ENERGY COALITION

1. These are the submissions of the School Energy Coalition ("SEC") in respect of Phase II of Oshawa PUC Networks Inc.'s ("Oshawa" or the "applicant") 2009 rate application.

2. The sole issue to be decided in this phase of the proceeding is Oshawa's application for an incremental capital module pursuant to the Board's 3rd Generation Incentive Regulation formula ("3GIRM").

3. In SEC's submission, the application for an incremental capital module should be dismissed, for two reasons:

(a) Oshawa has not demonstrated that its' capital budget, taken as a whole, meets the eligibility criterion for incremental capital module as set out in the Board's 3GIRM Report; and

(b) the four specific "incremental" projects for which Oshawa has applied for funding do not meet the criteria in that they are either not non-discretionary and/or represent expenditures designed to increase productivity, which are not, in SEC's submission, properly the subject of an incremental capital module.

i.) Calculation of Eligible Incremental Capital Amount

4. To begin with, SEC would like to set out what it believes is the amount by which Oshawa's total 2009 capital budget exceeds the threshold amount set out in the 3GIRM. This is the amount which would be is *eligible* for a capital module, assuming Oshawa meets the other elements of the test.

5. SEC calculates the total as follows:

Gross 2009 capital spending		$16,799,464
Less:	Amount carried over from 2008	$1,700,000[1]
Net 2009 Capital Spending		$15,099,464
Less:	Smart meter spending	$4,851,144
	Update to Concrete Pole Project	$1,311,800
Total capital adjusted 2009 capital spending:		$8,936,520[2]
Less:	Threshold amount	$6,695,123[3]
Total above materiality threshold		**$2,241,397**
Plus: correction for 2008 capital spending		**$200,000[4]**
Total above materiality threshold		**$2,441,397**

6. The total amount by which Oshawa's 2009 capital spending exceeds the materiality threshold, therefore, is $2,441,397. This slightly exceeds the amount of additional capital spending for which Oshawa seeks recovery, $2,221,500 [see Board Staff IR#1(g), p. 10 of 25].

ii.) Total Capital Budget Includes Discretionary Items

7. SEC participated in the consultation process leading up to the development of the Board's 3GIRM formula. In its Report the Board established that the 3GIRM would be a multi-year rate-setting plan which included a comprehensive price cap adjustment mechanism. The price cap mechanism contained a built-in adjustment for inflation and productivity. The Report contained two exceptions of costs that would flow through to rates in addition to the price cap formula: a z-factor limited to events genuinely external to the regulatory regime and beyond the control of management; and a incremental capital module that is subject to eligibility criteria and a materiality threshold.

8. In approving the incremental capital module, the Board stated that the module would be the exception to the norm:

> The Board has determined that there will be an incremental capital module in 3rd Generation IR. Distributors with an amount of capital

[1] As explained in cross-examination and in response to UTJ1.2, this amount was already excluded from the capital expenditure summary provided in response to Board Staff IR#1(e) [p. 7 of 25]. The net amount, $16,799,464 minus $1,700,000, equals $15,099,464 is the same total as that shown in the response to Board Staff at p. 7.

[2] A similar number, based on a rough calculation, was put to the witnesses in cross-examination at Tr1:73-74.

[3] This is the updated threshold amount provided in response to UTJ1.1.

[4] This is related to Oshawa's response to Undertaking J1.3, wherein it states that its 2008 capital spending was actually $1.5 million below forecast, not $1.7 million shown in the evidence. SEC has added the $200,000 at the end of this table so that the rest of the numbers ($15,099,464, etc.) remain consistent with those shown in the evidence.

> spending that exceeds the materiality threshold may best be accommodated through rebasing. However, on balance, as participants acknowledged, some incremental capital investment needs may arise during the IR term and the Board notes that a clearly defined modular approach is generally accepted.
>
> [Report of the Board dated July 14, 2008, p.33]

9. The Board then set out the eligibility criteria that distributors must meet in order for their incremental capital requirements to be considered for recovery in rates prior to rebasing:

Criteria	**Description**
Materiality	The amounts must exceed the Board defined materiality threshold and clearly have a significant influence on the operation of the distributor; otherwise they should be dealt with at rebasing
Need	Amounts should be directly related to the claimed driver, which must be clearly non-discretionary. These amounts must be clearly outside of the base upon which rates were derived.
Prudence	The amounts derived must be prudent. This means that the distributor's decision to incur the amounts must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.

Report of the Board, p. 33.

10. In SEC's submission, ICM was meant to provide rate relief for utilities facing capital expenditures which are, in total, both in excess of the materiality threshold and non-discretionary. As such, the eligibility criterion applies to a distributor's entire capital budget, not just the projects that the utility defines as "incremental".

11. What Oshawa has done in this proceeding, in SEC's submission, is taken four projects which it states are the "incremental" projects and applied for an incremental capital module on the basis of those four projects.

12. SEC disagrees with this approach, and submits that, in deciding whether a utility meets the eligibility criterion, the Board must examine the utility's total capital budget for the rate year.

13. SEC therefore asked for information on the Applicant's entire 2009 capital budget. A synopsis of the 2009 projects was provided in response to Undertaking J1.6. Although the list provided by Oshawa identifies every project as "non-discretionary", an examination of the information provided reveals that several in fact appear to be discretionary. Projects C08-203 ($308,000), C08-211 ($285,600), and C08-290 ($800,00), for example, are all related to "system planning for growth in the NE area." The description for these projects demonstrates that their timing is discretionary. Oshawa states for example, with respect to projects C08-203 and C08-211: "Oshawa is experiencing growth in the NE area of its service territory. By completing the work on this circuit the construction of a new municipal substation can be delayed." [J1.6, p. 3]

14. In addition, the filing requirements for the Incremental Capital Module set out in the Board's Supplementary 3GIRM Report[5] requires that distributors provide "evidence that the incremental revenue requested will not be recovered through other means (e.g. it is not, in full or in part, included in base rates or being funded by the expansion of service to include new customers and other load growth." It appears that some of the projects discussed above fall into this category, in that they are undertaken to facilitate an expansion of service, and would therefore result in incremental revenue for the utility.

ii.) Three of the "Incremental" projects are not non-discretionary

15. Oshawa has applied for funding for four specific projects which, it says, are responsible for its capital budget exceeding the materiality threshold thereby making it eligible for an incremental capital module. The four projects are:

(a) Concrete Pole Replacement ($210,000);

(b) Long-Term Load Transfer ($907,500);

(c) Distribution System Reliability ($850,000);

(d) Mobile Work Force ($254,000).

(a) Concrete Pole Replacement ($210,000)

16. SEC agrees that the Pole Replacement project is non-discretionary in that it involves a potential safety issue and therefore must be addressed in 2009. However, the cost of this project is offset by other projects in Oshawa's 2009 capital projects discussed above which are not non-discretionary.

(b) Long-Term Load Transfer ($907,500)

17. With respect to the long-term load transfer, the company's pre-filed evidence states that the "project is required under regulation and as such is clearly non-discretionary." [see Manager's Summary, p. 9] It is clear from this description that the basis upon which Oshawa described the project as non-discretionary was the previous regulatory requirement that it be completed by January 31, 2009.

18. That requirement no longer exists. In SEC's submission, the following exchange between Mr. Buonaguro and Mr. Mahajan demonstrates that this project is now completely discretionary:

> MR. BUONAGURO: Now, you talked about the long-term load transfer project … [a]nd to summarize my understanding, when

[5] EB-2007-0673, Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, dated September 17, 2008 (the "Supplemental Report"), Appendix B, p. VI-VII.

you originally applied, you had a deadline of January 31st 2009; correct? And you applied –- at the same time you were working under that deadline you applied for and were granted an extension to 2011; is that correct?

MR. MAHAJAN: Yes, that is correct.

MR. BUONAGURO: And then you acknowledged in your chief -– your in-chief evidence that the Board has recently proposed an amendment pushing the date out to 2014 for all distributors.

MR. TURNEY: That's correct. The end of June 2014.

MR. BUONAGURO: Okay. Now, you may be revisiting some of your comments in-chief, but doesn't that mean that you have the discretion to rework this plan for a term of five years as opposed to the first month of 2009?

MR. MAHAJAN: That's true. *I mean we do have that discretion*, but like I -– like I said in the opening remarks that there are other drivers beside the regulatory driver, in terms of building the reliability in the system and also ensuring, as Mr. Turney had mentioned in his comments, that it would help us service the thousand-odd customers.

[Tr1:51]

19. Mr. Mahajan went on to say that the "other drivers" are related to enhancing the reliability of the system:

MR. MAHAJAN: I think it's not a question of degradation of reliability. It's a question of enhancement of reliability, because we will be picking up new customers, as Mr. Turney said, in that part of Oshawa, which would help us build some redundancy by completing that loop. That allows us to enhance the reliability for our customers, so it's not a question of degradation. It's a question of enhancement of reliability.

[Tr1:52-53]

20. However, when asked why the company asked for the extension in the first place, the company replied that because of "resource constraints" [Tr1:91].

21. Mr. Mahajan was then asked why the company continued to seek funding for the project in this application, given that it had asked for and received permission to defer the project. Mr. Mahajan's response was that the company now wished to go ahead with the project because there is now a mechanism available for recovery of the cost- i.e. the incremental capital module. [Tr1:91]

22. In SEC's submission, however, the purpose of the capital module is not to allow a utility to accelerate a project that the utility itself had asked to be deferred when there was no capital module. If the company believed when it applied for the extension that the project did not need to be completed in 2009 then that is a strong indication, in SEC's submission, that the project is not non-discretionary. The only reason the company now seeks to accelerate the project is because the capital module exists to provide funding. In SEC's submission, projects should not be driven by the fact that a capital module exists to provide funding.

c.) Distribution System Reliability ($850,000)

23. The purpose of this project is to replace a specific distribution feeder identified as a poor performer [Manager's Summary, p. 10]. Oshawa states that replacing the feeder would mean that "overall reliability statistics for the OPUCN distribution system will be improved significantly." [ibid.].

24. In SEC's submission, like the long-term load transfer project discussed above, this project also appears to be driven by the existence of an incremental capital module and does not appear to be non-discretionary.

25. In the Manager's Summary, for example, Oshawa states that as follows:

> The base capital construction plan for 2009 contains other projects designed to increase system reliability. However, staffing restrictions and the demands placed on our construction capabilities by continued development dictate that OPUCN cannot undertake as many reliability enhancement projects as would be consistent with our commitment and direction to increase system reliability. *An Incremental Capital allowance for this project would allow OPUCN to prudently hire third party contractors to accelerate efforts aimed at improving system reliability to acceptable levels*.
>
> [Manager's Summary, p. 11; emphasis added]

26. The last sentence appears to indicate that the company has decided to pursue this project at this time because of the existence of the capital module.

27. This is confirmed in a response to a Board Staff interrogatory, where Oshawa states that this project did not initially "make the 2009 list [of capital projects] through the regular process as there were insufficient funds available to complete the project, resulting in the project being pushed off of the list. Funding through the IRM adjustment process will allow this much needed project to be completed in 2009." [Board Staff IRR#12(c)].

28. In SEC's submission, Oshawa's position misconstrues the intent of the incremental capital module. Oshawa's position is similar to that put forward by the distributors during the consultation process leading up to the development of the 3GIRM framework and the

incremental capital module. The Board rejected the distributors' view of the intent of the incremental capital module and appears to have preferred that of the ratepayers:

> The Board notes that there are clearly differences in perception as to the purpose of the incremental capital module. Ratepayer groups perceive the capital module as a mechanism aimed solely at addressing extraordinary or special CAPEX needs by distributors. *The distributors, on the other hand, perceive the module as a special feature of the 3rd Generation IR architecture which would enable them to adjust rates on an on-going, as-needed basis to accommodate increases in rate base*.
>
> In the Board's view, *the distributors' view is <u>not</u> aligned with the comprehensive price cap form of IR* which has been espoused by the Board in its July 14, 2008 Report. The distributors' concept better fits a "targeted OM&A" or "hybrid" form of IR. This alternative IR form was discussed extensively in earlier consultations but was not adopted by the Board. The intent is *not to have an IR regime under which distributors would habitually have their CAPEX reviewed to determine whether their rates are adequate to support the required funding. Rather, the capital module is intended to be reserved for <u>unusual circumstances</u> that are not captured as a Z-factor and where t<u>he distributor has no other options</u> for meeting its capital requirements within the context of its financial capacities underpinned by existing rates*.
>
> [Supplementary Report, p. 30-31; emphasis added]

29. In SEC's submission, projects that the utility had previously deferred due to resource restrictions, and for which it is now applying for funding on the basis that a capital module exists, would be more appropriate in the type of capital module that would have existed had the Board accepted the distributors' concept of a capital module. The Board clearly and, in SEC's submission, justifiably, rejected that view as being at odds with an incentive regulation framework.

<u>d.) Mobile Work Force ($254,000)</u>

30. This project is driven by Oshawa's commitment to "continuous improvement in the operation of its distribution system business." [Manager's Summary, p. 12]. The project involves the "purchase of a mobile workforce system in 2009 that allows office staff to issue work to field staff via a remote link and tablet computer system [Manager's Summary, p. 13]. The system would replace the current, manual-based, system.

31. When asked how this project met the test of "clearly non-discretionary" Oshawa replied as follows:

> Oshawa is expecting a large number of retirements in the next five to ten years. We need to turn to technology to find efficiencies based on equipment such as this to absorb these manpower reductions without compromising reliability and safety.
>
> [Board Staff IR#17(a).]

32. In SEC's submission, this project is clearly driven by a desire to achieve efficiencies within the distribution system. In fact, the company has identified cost savings that will be achieved within the IRM period of approximately $88,375 per year. SEC notes Mr. Mahajan's contention that these savings would not occur "overnight" [Tr1:94]. However, it is very likely they will be achieved within the IRM period. The savings will obviously not be passed on to ratepayers during the IRM period.

33. In SEC's submission, therefore, this is precisely the sort of project that the Board contemplated would be undertaken, and funded, by utilities during the IRM period. It will improve the efficiency of the system and therefore yield cost savings for the utility. It is not, in SEC's submission, the sort of project that was contemplated as being eligible for an incremental capital module.

<u>Regulatory Costs</u>

34. With respect to Oshawa's claim for regulatory costs associated with this proceeding, SEC submits that there is no mechanism within the 3GIRM framework to recover operating expenses that do not meet the z-factor threshold. There is, in SEC's submission, a very good reason for that: allowing a utility to apply for special funding for one particular area of costs that have increased amounts to single-issue rate making; it ignores the fact that other costs may have decreased from their forecast level, the savings from which would not be passed on to ratepayers.

35. In fact, even in the specific area of regulatory costs there is an indication that the level of costs currently being recovered by Oshawa in rates may be greater than their actual level. As Board Staff points out, the approved level of regulatory costs included in Oshawa's base rates, $53,000, was based on an assumption that the total cost would be amortized over a three-year IRM period. It now appears that Oshawa will not be re-based until 2012, which means that the proper amortization period would have been four years instead of three. This means that Oshawa will recover $212,000 for its 2008 cost of service application ($53,000 included in 2008 base rates times four years) even though it had estimated the expense to be $150,600.

36. In SEC's submission, therefore, company's proposed regulatory costs variance account would amount to single-issue rate making and should be rejected.

<u>Costs</u>

37. SEC participated responsibly in this proceeding and sought to contribute to the Board's understanding of the issues while cooperating with other ratepayer groups to minimize costs. SEC therefore respectfully requests that it be awarded 100% of its reasonably incurred costs.

Respectfully submitted this 4th day of May, 2009.

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