EB-2009-0180
EB-2009-0181
EB-2009-0182
EB-2009-0183

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 pursuant to section 60(1) of the *Ontario Energy Board Act, 1998* by 1798594 Ontario Inc. seeking an electricity distribution licence;

AND IN THE MATTER OF an application pursuant to section 86(1)(a) of the *Ontario Energy Board Act, 1998* by Toronto Hydro Energy Services Inc. seeking an order granting leave to sell streetlighting assets as an entirety or substantially as an entirety to 1798594 Ontario Inc.;

AND IN THE MATTER OF an application pursuant to section 86(1)(b) of the *Ontario Energy Board Act, 1998* by Toronto Hydro Energy Services Inc. seeking an order granting leave to sell streetlighting assets necessary in serving the public to 1798594 Ontario Inc.;

AND IN THE MATTER OF an application pursuant to section 86(1)(c) by Toronto Hydro-Electric System Limited and 1798594 Ontario Inc. seeking leave to amalgamate;

AND IN THE MATTER OF a request pursuant to section 77(5) of the *Ontario Energy Board Act, 1998* by 1798594 Ontario Inc. seeking the cancellation of the distribution licence applied for in a separate application under section 60(1) of the *Ontario Energy Board Act, 1998;*

AND IN THE MATTER OF an application pursuant to section 18(2) of the *Ontario Energy Board Act,* 1998 by 1798594 Ontario Inc. and Toronto Hydro-Electric System Limited for an order assigning Toronto Hydro-Electric System Limited's electricity distribution licence to a proposed amalgamated entity consisting of 1798594 Ontario Inc. and Toronto Hydro-Electric System Limited.

Final Argument of the

School Energy Coalition

1. The following are the final submissions of the School Energy Coalition ("SEC") in relation to the applications filed by Toronto Hydro-Electric Systems Limited ("THESL") and various affiliated companies for an order approving the a series of transaction designed, ultimately, to transfer the streetlighting assets currently held by Toronto HYdro Electric Services Inc. ("THESI") to THESL.

2. As set out in greater detail below, SEC, with the exceptions noted below, is opposed to the application for the following reasons:

(a) With the exception of some of the conductors and conduits that are currently part of the streetlight system, the Applicants have not demonstrated that the streetlight assets constitute a distribution system. The Applicants' proposed definition of a distribution system could apply to myriad other electrical systems and expand the Board's regulatory powers into areas not contemplated by the Legislature. Any assets that are not part of the distribution system are, in our submission, not regulated assets and cannot be acquired and operated as regulated assets by the regulated utility.

(b) SEC believes that the applicants have not demonstrated that the proposed transaction meets the no harm test. As a result of the transaction, streetlighting and USL distribution customers, and possibly other customers as well, will pay more for their distribution rates to make up for the deficiency in operating the streetlight business on a rate-regulated basis;

(c) The Applicants propose to charge a price for the streetlighting service that is not rate-regulated. That is contrary to the requirements of the OEB Act.

(d) Finally, the Applicants have not provided a proper valuation of the assets to determine their net book value. The Valuation prepared by Deloitte, which was the basis for the purchase price paid by THESI, was a fair market value valuation the assets and does not represent net book value. In addition, the value of the assets was much greater in the 2005 transaction as a result of the more restricted assumption of liabilities clause.

I. Definition of Distribution Assets

3. It appears from the evidence that both THESI and THESL have treated as distribution system parts of the system that are in reality owned by THESI. The basis for this, and the basis for the current application, is that some parts of the streetlighting system are connected not just to streetlighting load, but to third party load, such as Bell telephone booths, decorative lighting, and billboards, as well [see, for example, Tr1: 13-15].

4. The Ontario Energy Board Act states that "distribute", with respect to electricity, as "means to convey electricity at voltages of 50 kilovolts or less."

5. That definition, however, could have potentially unlimited application unless the word "convey" is qualified in some fashion.

6. SEC submits that that analysis should be informed by the underlying purpose of the Board's regulatory power: to regulate the rates charged by monopoly providers of an essential service. The distribution system should not include end uses and should not include assets whose sole purpose is to serve a single end use.

7. In that respect, SEC has reviewed the proposed demarcation points for distribution assets set out in the Final Argument of the Electrical Contractors Association of Ontario and the Greater Toronto Electrical Contractors Association, specifically paragraph 11 thereof. SEC agrees with that definition. Under that definition, it would appear that certain of the underground and overhead conductors and underground conduits would be considered distribution assets and transferred to THESL, whereas the poles and fixtures would not.[1]

8. With respect to the fixtures specifically, it appears that the Applicants witnesses accept that they are load just like other elements of the streetlight system such as the TTC bus shelters or Bell telephone booths. They have been included as part of the application for the sake of convenience [see Tr1:50, 175].

9. During re-direct examination, the Applicants' counsel put to the witnesses the proposition that the "given the Green Energy Act requirements, and now this Board's directives about implementing smart grid for Ontario, that it might be possible that new technologies could be developed that create devices that increase or enhance lumen efficiency of streetlighting?" The witnesses agreed that they would.

10. The Applicant then argued that the fixtures, though load, fit within the exception to the activities that a regulated distributor may undertake. The exception the Applicants refer to states as follows:

> Restriction on business activity
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> **71.** (1) Subject to subsection 70 (9) and subsection (2) of this section, a transmitter or distributor shall not, except through one or more affiliates, carry on any business activity other than transmitting or distributing electricity. 2004, c. 23, Sched. B, s. 12.
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> Exception

[1] See Ex. F-20-3 for a breakdown of the value of the assets, as of December 31, 2008, by category. But see SEC submissions below regarding the valuation of the assets generally.

> (2) Subject to section 80 and such rules as may be prescribed by the regulations, a transmitter or distributor may provide services in accordance with section 29.1 of the *Electricity Act, 1998* that would assist the Government of Ontario in achieving its goals in electricity conservation, including services related to,
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> (a) the promotion of electricity conservation and the efficient use of electricity;
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> (b) electricity load management; or
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> (c) the promotion of cleaner energy sources, including alternative energy sources and renewable energy sources.

11. The construction the Applicants place on that exception, however, is that the asset falls within the exception if it is possible to make that asset more efficient. That definition, however, would mean that any asset that could be made more energy efficient could be a distribution asset. Any light with, say, a light sensor designed to conserve its use could be a distribution asset.

12. That cannot, in SEC's submission, have been the intent of the Legislature in developing the exception. Rather, SEC submits that the proper interpretation of the exception is that assets whose purpose is to promote the efficiency of other assets, either in the distribution system or load attached to the system, could be "distribution assets" even if they are not used to convey electricity.

13. In addition, there is no evidence that the assets need to be part of the distribution system in order for the efficiencies the Applicants discussed to materialise. The THESI witness on the panel, for example, explained to the Board that THESI is already undertaking a number of efficiency measures in respect of the luminaires. Mr. Cook described, for example, a program that THESI is currently running called ALAMP (Adaptive lighting Asset Management Project) that is designed to adapt the amount of light on a roadway according to "pedestrian conflict" [see Tr2:99-100] . The fact that THESI is already undertaking these measures contradicts the view, implicit in the Applicants' argument, that including the assets in the regulated rate base is the only way to promote efficiency.

Other Issues

14. In addition to the above, SEC submits that there are problems with the application that have not been addressed.

i. No Harm Test Not Satisfied

15. The Applicant has stated that, as a result of transferring the streetlight assets into THESL and applying a rate-regulated rate of return on them, there will be a deficiency,

between the amount collected and the revenue requirement in respect of the assets, of approximately $350,000. The Applicant's proposal is that that deficiency be allocated to the Streetlight and USL rate classes.

16. Most of the members of these rate classes are currently customers of THESI for the provision of streetlighting service. The City of Toronto, for example, has a long-term contract with THESI for the provision of streelighting service with a pre-determined annual price. Other customers may have similar contracts. What is clear is that, for all of them, while the price they currently pay for the provision of streetlighting services will nominally stay the same, in reality they will be paying more for the service as a result of this transaction. That is, though styled as distribution rate increase, which itself is non-compliant with the non-harm test, the $350,000 deficiency is in reality an incremental cost for the provision of what would now be the regulated streetlighting service.

17. In addition, in the event the costs to service the streetlighting assets increase in the future- due, for example, to aging infrastructure, increased liability claims, or other factors, those costs will be passed on to the streetlighting customers, whereas under the current arrangement they are THESI's responsibility. The risk of those cost increases, therefore, is being transferred from THESI to THESL's distribution customers without compensation.

18. In addition, there is no guarantee that the costs will be restricted to streetlighting and USL customers. To the extent that the streetlighting assets were or are in the future, involved in an incident similar to the contact voltage incident, part of all of the costs may be allocated to all ratepayers. That was the case with respect to the extended remediation costs stemming from the Contact Voltage Level III Emergency [Undertaking J2.1].

19. In some cases, it may be difficult to even identify the costs that stem from the streetlight assets. For example, in the event that THESL's liability insurance rates increase in the future as result of the increased liability (more on the assumed liabilities below) of the streetlight assets, it would be difficult to allocate that increase to a single rate class.

ii.) No "Just and Reasonable Rate" for Streetlighting Service

20. Section 72(2) of the OEB Act, 1998 states that "no distributor shall charge for the distribution of electricity…except in accordance with an order of the Board, which is not bound by the terms of any contract."

21. If the streetlighting assets are deemed to be distribution assets, then THESL cannot as a matter of law charge for the streetlighting service except in accordance with an order from the Board. As a practical and legal matter, the rates charged for lighting the streets of Toronto, and perhaps as this is extended for providing traffic lights and other such loads, will have to be set by the Board.

22. The THESL witnesses suggested during cross-examination that, for now, the contract rates should be treated as a revenue offset and that, in the future, "we could conceive of a

situation where…there is a streetlight rate class which has the distribution costs, and then a maintenance service rate charge." [Tr1:148].

23. If the Board were to accept the applications it would have to accept that the assets are distribution assets. In that case, any charge in respect of the asset would have to be a distribution charge. It could not be a revenue offset, as suggested by the THESL witness. The OEB Act requires that rates for distribution services be charged on a regulated basis, so if these assets are distribution assets, the service provided through them must be at regulated rates.

24. In order for the Board to make an order for a distribution charge, however, it would have to find that the proposed charges in respect of the streetlighting services are just and reasonable. But no information has been provided to justify the proposed rates that are currently set forth in the various streetlighting contracts (whether with the City of Toronto or other parties). The Board therefore has no evidence upon which to make a determination that the rates set out in THESI's service contracts constitute just and reasonable rates for the distribution of electricity.

25. The THESL witness admitted as much when he said, in answer to Board Member Quesnelle's question, that in the future the revenue offset could be replaced by "a full cost of service underneath it that would then say, here are the services that make up that charge." [Tr1:153]

26. What the Applicants are proposing, therefore, is a distribution asset without a distribution rate. SEC respectfully submits that the OEB does not have jurisdiction to include in rate base assets that are not subject to regulated rates.

iii.) No Proper Valuation of Assets

27. The Board's policy is that only the net book value of assets may be included in a regulated utility's rate base.

28. THESL states that the net book value of the streetlight assets is $62.5 million. That value is derived by taking the price, $60 million, that THESI paid the City of Toronto for the assets in 2006 and adjusting it for additions and depreciation since that date [see, for example, Exhibit F, Tab 19, Schedule 1, pg. 2].

29. The $60 million purchase price, however, does **not** represent the net book value of the assets as of December 31, 2005.

30. As THESL's witnesses testified, the $60 million purchase price was based on a valuation performed by Deloitte and Touche for Toronto Hydro Corporation in 2005. As noted by Deloitte's counsel's, however, that report was a fair market value valuation and was not prepared for the purposes to which THESL now purports to use it:

> Deloitte prepared the Report containing an estimate of the *fair market value*, as at October 31, 2005, of all of the fixed assets and business operations, considered together, of the City of Toronto's street and expressway lighting system (together, the "Business"). The Report was prepared in connection with Toronto Hydro Corporation's proposed acquisition of the Business, effective December 31, 2005. **Note that the Report, dated as at October 31, 2005, was not prepared for any other purpose and, specifically, was not prepared for the purpose of/in contemplation of the current proceedings before the Board or any of the issues raised therein. Therefore, the Report should NOT be relied on in any way by any third parties.**
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> [Covering email of Deloitte Counsel dated November 27, 2009; bold in original; italics added]

31. Even without referring to the specific report, therefore[2], it is clear that the valuation performed by Deloitte is insufficient to serve as the basis upon which the current proposed net book value is determined. A more detailed analysis of the report shows that the value chosen was considered appropriate for a business valuation. That is not appropriate for regulatory purposes.

32. In addition, the liabilities assumed by THESL are more extensive than those assumed by THESI. The current, proposed, Asset Purchase Agreement between THESL and THESI states as follows:

> 3.1 *Assumption of Liabilities by the Purchaser*. Subject to the provisions of this agreement, the purchaser agrees to assume, pay, satisfy, discharge, perform and fulfil, from and after the closing date, all of the obligations and liabilities, contingent, accrued, present and future, related to the SEL business, including those liabilities under all contracts related to the SEL business, including the city agreements and liabilities which are specified in Schedule 3.1.
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> [Exhibit C, Tab 7, para. 3.1]

33. By contrast, the original Asset Purchase Agreement between Toronto Hydro Street Lighting Inc. (whose rights and obligations thereunder were subsequently transferred to THESI) and the City of Toronto provides a far more limited assumption of liability provision.

[2] SEC intentionally will not refer to the actual report so as to avoid having to file a redacted version of its submissions.

> 3.1 *Assumption of **Certain** Liabilities by the Purchaser*. Subject to the provisions of this agreement, the purchaser agrees to assume, pay, satisfy, discharge, perform and fulfil from and after the effective date **only those obligations and liabilities which are specified in Schedule 3.1**."
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> [Asset Purchase Agreement between Toronto Hydro Street Lighting Inc. and City of Toronto; Exhibit F-21-12, Appendix A, paragraph 3.1; emphasis added]

34. Therefore, while in the initial transaction the purchaser, Toronto Hydro, assumed only a specific list of liabilities, in the current transaction THESL's potential liability is unlimited; it is essentially taking over all known and unknown liabilities associated with the streetlighting assets [see Ex. F-22-8 (a) and Tr1:160].

35. When asked in cross-examination about the two agreements, the Applicants' witnesses agreed that the former assumption of liability clause is much more restrictive than the one included in the current agreement. [Tr1:162]

36. The THESL witnesses added that the former agreement was done as an arm's length transaction between the City of Toronto and Toronto Hydro. Even if that were true, however, it suggests that Toronto Hydro, as an 'arm's length' purchaser of the assets, negotiated a far more restrictive assumption of liability clause than THESL, an affiliate of THESI, subsequently agreed to, even though the purchase price is the same.

37. Therefore, in addition to the problem that the 2005 valuation does not represent net book value, it was not even done on the same basis as the current transaction. The price/net book value of the assets would have to take into account the additional liabilities that come with the assets in this transaction as opposed to the 2005 transaction.

38. Aside from the valuation of the assets, the assumed liabilities also raise an important point about the risks to THESL ratepayers emanating from this transaction. The contact voltage incidents, and ensuing litigation, demonstrates that the liabilities associated with these assets could be could be significant.

39. Therefore, even if the transfer is accepted, SEC submits that the asset purchase agreement be required to be amended to provide that THESI indemnify THESL for liabilities emanating from the condition of the assets at the time of the transfer.

Costs

40. The School Energy Coalition participated responsibly in this proceeding and contributed to the Board's understanding of the issues. SEC respectfully requests that it be awarded 100% of its reasonably incurred costs.

All of which is respectfully submitted this 30th day of November, 2009.

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John De Vellis

Counsel to the School Energy Coalition