



Jay Shepherd

Professional Corporation
2300 Yonge Street,
Suite 806
Toronto, Ontario M4P 1E4

BY EMAIL and RESS

December 16, 2011
Our File No. 20110273

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
M4P 1E4

Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2011-0273 – Grimsby 2012 Rates

We are counsel for the School Energy Coalition. Pursuant to the Board's Procedural Order delivered orally on December 12, 2011, these are SEC's submissions with respect to the Application. Our submissions are limited to the one outstanding issue, the OM&A budget for the Test Year.

Background

1. The Applicant is seeking a revenue requirement and rates that include, after all adjustments, OM&A excluding property taxes totaling \$2,375,758 on a CGAAP basis, and \$2,536,566 on a MIFRS basis [Staff TC 12(c)]. This represents an increase over 2010 actual OM&A spending of 31.6% on a CGAAP basis, and 40.5% after taking the MIFRS increase into account.
2. The capitalization of overheads, which is a common feature of IFRS conversions, had an unusual twist in this case. Capitalization was changed twice instead of once.
 - a. First, the Applicant adjusted its capitalization under CGAAP because it determined that it was capitalizing too much. This resulted in an increase in OM&A of \$139,820 from 2010 to 2011, and a further increase of \$14,314 from 2011 to 2012, for a total



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adjustment upwards of \$154,134 [all from Table 4.8]. This is not a MIFRS adjustment.

- b. Second, the Applicant adjusted its capitalization in the conversion from CGAAP to MIFRS by a further \$160,808 [Staff TC 12(c)].

The net result is that these two changes, totaling \$314,942, are not an increase in spending, but a reallocation from capital to OM&A. To put this on an apples to apples basis relative to 2010 (i.e. unadjusted CGAAP), Test Year OM&A would be \$2,221,624, which is a 23.0% increase over 2010, and the agreed Test Year capital expenditures would be \$1,702,591, which is a 16.7% increase over 2010.

3. SEC has no concerns with respect to the conversion of Test Year OM&A from CGAAP to MIFRS. Therefore, the balance of these submissions refer only to CGAAP unless the context otherwise states.
4. All of the above numbers are subject to adjustment for the responses to the undertakings, filed December 14th. There are two key adjustments in those responses.
5. First, Ex. J1.2 provides a new Table 4.24 (i.e. Appendix 2K) in which the compensation allocated to OM&A is reduced by \$110,974. There is no explanation of how this integrates with the total OM&A budget requested.
6. Second, Ex. J1.4 shows that the current Test Year forecast of two categories – Seminars and Conferences and Training and Educational - is \$34,254, which is about \$40,000 less than the amount included in the budget approved by the Board of Directors [Tr.1:59 on the public record, and Tr. 1:52 in camera] and included in the Application.
7. Our best estimate is that the OM&A cost driver table included in the Application as Table 4.8 is that it should now read as follows:

Cost Driver Table

	<u>2011</u>	<u>2012</u>	
Opening Balance	1,805,716	2,080,519	
(1) Staffing (Payroll and Benefits)	42,270	101,115	Undertaking J1.2
(2) Change in Allocation Method	139,820	14,314	
(3) Third Party Service Providers	12,744	44,114	Undertakings J1.3, J1.4
(4) Smart Meter System Costs	0	51,484	BS IR 15
(5) Computer Network and Website	0	28,568	
(6) Meter Maintenance	52,500	(-31,922)	
(7) LEAP Program	3,974	143	
(8) HST Saving	0	(-29,963)	BS IR 55b
(9) Remaining Balance	<u>23,495</u>	<u>117,386</u>	
Closing Balance	2,080,519	2,375,758	



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8. In preparing the above table, we have benefitted from seeing draft analysis from Energy Probe, including the revisions above. We have added one further revision, to increase the adjustment described in para. 6 above from \$16,912 [from Ex. J1.4, i.e. \$32,071 minus \$14,159] to \$40,133, which SEC calculates is the full impact of the difference between original budget of \$74,387 [Tr.1:52] and current forecast of \$34,254 [Ex. J1.4, p. 16].

Submissions

9. ***Need for Increased Spending.*** The argument of the Applicant is that Grimsby was underspending in the past, due to the establishment of a top-down budget that left insufficient room for necessary spending [Tr. 1:16-20]. Mr. Curtiss provided examples of this in his oral testimony, and the OM&A per customer comparison between this utility and others in its cohort showed its low spending.
10. The Board will be aware that SEC regularly compares overall rates and distribution bills across utilities, in order to diagnose where problems might be occurring. We note that, while we do not have a detailed comparison to provide, it is clear that Grimsby's existing (i.e. 2011) distribution bills are on average in the bottom 20% in the province. While having low rates should generally be a good thing, it can also be evidence that the utility is neglecting some aspects of its operations in order to save money. This would be consistent with the evidence of Mr. Curtiss. It is not in the ratepayers' interests to allow such a situation to continue.
11. ***Exceptional Level of Proposed Increase.*** On the other side, what is proposed is a very large increase, much more than the Board has ordered for almost any other utility. It is a dangerous precedent, and the Board should be concerned that other utilities will see this as a sign that they can or should seek substantial rate increases on rebasing. They may even feel that this decision encourages them to do so.
12. This is exacerbated by the likelihood that at least some of the proposed spending must be to catch up for underspending in past years. While the Applicant cannot assist with how much of the proposed spending will be in this category, it is clear that some is [Tr.1:61]. Thus, Mr. Curtiss says that the proposed OM&A budget is the new sustainable level, but also admits that it probably includes some catchup spending.
13. As a general principle, it is our view that a utility should not be free to cut back on spending in IRM years, in order to maximize ROE, and then on rebasing catch up that backlog with an increased budget for the ratepayers to fund.
14. The result is that, even if the Board agrees, as we do, that management is doing the right thing at Grimsby Power, funded by these spending increases, some part of the increase is spending that should have been incurred in prior years, funded by the rates already paid by ratepayers in those prior years.
15. ***Proposed Result.*** The Background section of these submissions demonstrates that there now remains an unexplained increase in OM&A from Bridge to Test Year of \$117,386, amounting to a 5.6% increase in OM&A by itself.



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16. We are aware that other parties will propose formulae based on percentage increases from past years (an “envelope” approach), and we have had an opportunity to review those numbers. We do see merit in those proposals.
17. However, in this particular case, in our view the Board could reach the optimal result simply by excluding from the approved CGAAP OM&A the \$117,386 “miscellaneous” increase that is unsupported for the Test Year. This would produce an OM&A figure under CGAAP of \$2,258,372, which is still an increase of 25.1% over 2010 actual, and 16.5% over 2010 actual after adjusting for the non-MIFRS capitalization change (i.e. \$2,104,238 in 2012 net of the cap change, compared to \$1,805,717 Actual for 2010, both calculated on the same basis).
18. In our submission, a 16.5% increase over two years, after making all adjustments, and even accepting that OM&A was underspent in prior years, is enough to operate this utility at a high standard. The resulting OM&A per customer, \$215.37, while still the lowest of the cohort, would be higher than many other utilities in the province. It therefore, in our view, is indicative that this result strikes the right balance between allowing a sizeable increase to catch up, and still maintaining an appropriate spending discipline.

Conclusion

19. It is therefore submitted that the Applicant's OM&A for the Test Year should be set at \$2,258,372, with revenue requirement and rates established on that basis.
20. SEC submits that it has participated in this proceeding in a responsible manner with a view to maximizing its assistance to the Board. It therefore requests that the Board order payment of its reasonably incurred costs of participation.

All of which is respectfully submitted.

Yours very truly,
JAY SHEPHERD P. C.

Jay Shepherd

cc: Wayne McNally, SEC (email)
Interested Parties