EB-2011-0271

ONTARIO ENERGY BOARD

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

AND IN THE MATTER of an Application by Halton Hills Hydro Inc. for an Order or Orders approving just and reasonable rates and other service charges for the distribution of electricity to be effective May 1, 2012.

FINAL ARGUMENT
ON BEHALF OF THE
SCHOOL ENERGY COALITION

April 13, 2012

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1 GENERAL COMMENTS

1.1 *Introduction*

1.1.1 This is the Final Argument of the School Energy Coalition ("SEC").

1.1.2 On August 26th, 2011, Halton Hills Hydro Inc. ("HHHI" or the "Applicant") filed an application for distribution rates, effective May 1, 2012, on a cost-of-service basis. The process included extensive interrogatories, a technical conference, settlement conference, and an oral hearing.

1.1.3 A Partial Settlement Agreement was filed with the Board on February 28, 2012, and was accepted by the Board at the commencement of the oral hearing held on March 22, 2012.

1.1.4 The ratepayer groups who intervened in this proceeding have worked together throughout the hearing to avoid duplication. Where SEC is in agreement with specific submissions of other parties, we have avoided repeating their arguments, but have instead adopted their reasoning.

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1.2 *Overview of Submissions*

1.2.1 ***General Comments.*** In its Argument-in-Chief the Applicant relies on the fact that the revenue deficiency is only $79,360, and that should be considered a reasonable increase. The applicant states that:

> The bottom line is that what HHH is asking for in relation to the unresolved issues is a very modest – almost negligible – increase in rates. That is the context for the disposition of the unresolved issues.[1]

Further, the Applicant seems to suggest that the decrease in the revenue deficiency since the filing of the Partial Settlement Agreement due to the Board's updated cost of capital parameters should influence the Board to consider the increases sought as being reasonable.[2]

1.2.2 SEC fundamentally disagrees with these propositions. A cost-of-service hearing is not

[1] Argument-in-Chief at para 8.
[2] *Ibid*, at para 5,7.

a proceeding for the purpose of increasing rates, it is to set "just and reasonable" rates pursuant to s.78 of the *Ontario Energy Board Act, 1998*. Where, as here, there are reductions in third party costs, it should not simply be assumed that these reductions can be added to other budget areas, since the overall increase is still small. If those other cost areas do not need that additional budget, it should not be approved. Further, while the rate-setting process often does lead to a rate increase that is not, and should not be, an inherent characteristic of the process.

1.2.3 ***OM&A.*** The Application proposes an increase in OM&A expense spending for the Test Year of 28.8% over the Bridge Year and 33.8% over 2010 actuals. In SEC's submission, this is far in excess of a reasonable amount. SEC submits that an appropriate amount for the Test Year is $5,124,500, a 14.5% increase over 2010 actuals.

1.2.4 ***Green Energy Initiative.*** The Applicant's proposal to install solar panels on 1400 of its poles is best characterized as a pilot project. Since the net present value is not to the benefit of ratepayers, the Board should only approve 10% of the proposed expenditures so that the Applicant may undertake a more in-depth pilot project to determine if the non-economic benefits warrant such a large expenditure.

1.2.5 ***PP&E Deferral Account Disposition.*** The Applicant is seeking an unprecedented 20-year amortization term for the disposition of the balance in its PP&E Deferral Account. SEC submits that the Board should allow no more than a 4-year amortization period. Further, the calculation of the balance and the annual impact should be reviewed and, if necessary, adjusted.

1.2.6 ***Long-Term Debt.*** During the course of the discovery process, it was revealed that two additional debt instruments are to be utilized by the Applicant. Adjusting in part for that, SEC submits the correct long-term debt rate to be applied is 3.85%

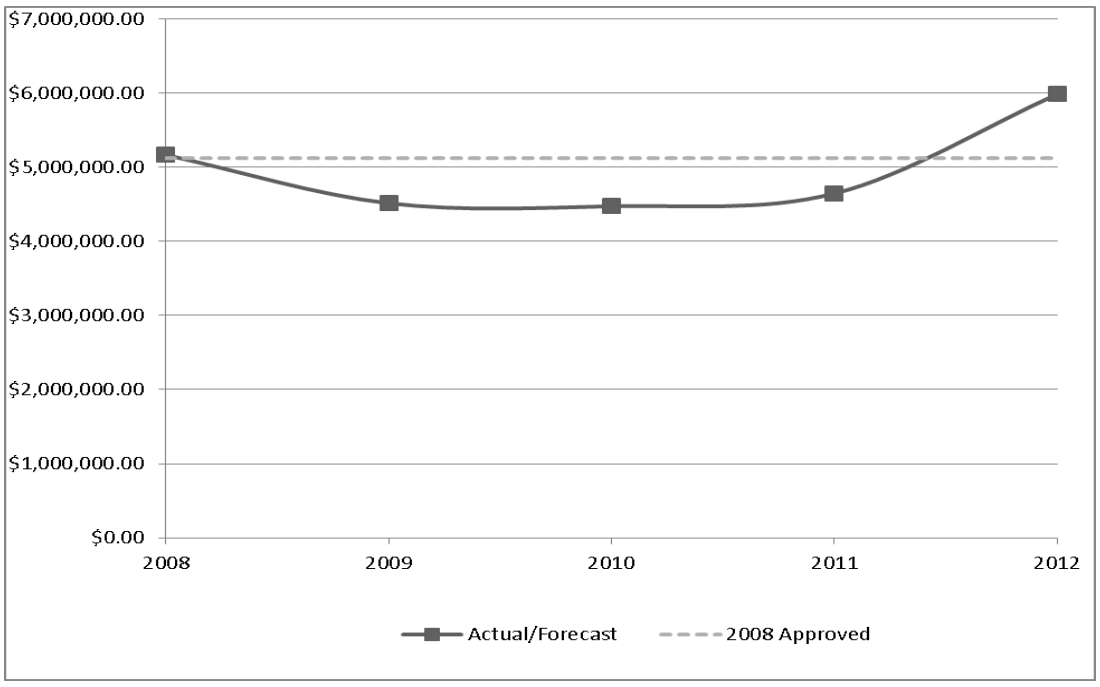
2 OM&A

2.1 *Overall OM&A Expenses*

2.1.1 The Applicant is proposing that rates be adjusted to increase the amount for OM&A expenses from the current amount on which rates are based (in CGAAP) to $5,987,400, a substantial increase. As discussed below, SEC submits that the appropriate total OM&A budget for the Test Year is $5,124,500, which represents a 14.5% increase over 2010.

2.1.2 SEC believes it is important to look at the 2010 actual OM&A spending, due to multi-year consistent under-spending by the Applicant that has occurred during the IRM term. In each of 2009, 2010 and 2011, the Applicant underspent their approved OM&A by a significant amount.

2.1.3 While a major feature of the IRM regime is that any gains from productivity or from decreasing costs during that period should flow to the utility and its shareholder as an incentive, those gains should be sustained, and during rebasing flow on a prospective basis to ratepayers. The gains that directly benefit the shareholders of the Applicant during IRM are not supposed to disappear during rebasing.



2.1.4 During the oral hearing, Mr. Skidmore attributed much of the decrease in OM&A spending during the IRM period to organizational change, which included a "flattened organization" in which there are fewer VPs and now a more professional management structure.[3] SEC submits that the Applicant should be praised for these changes. The Applicant has been able to lower its overall employee count and cost, while having both no reductions in service quality, and maintenance of all material standard utility practices.[4] Now the Applicant states that it must add four FTEs in the Test Year, and seven since 2010. This is just one example of some of those reductions and productivity gains during the IRM term that are said to have disappeared now that the Applicant is before the Board in a cost-of-service hearing. Surely they do not all disappear at the end of the IRM.

2.1.5 SEC submits that a just and reasonable OM&A expense that the Board should approve is $5,124,500, which is 14.5% increase over the Applicant's 2010 actuals. The number was derived by applying the amount that was awarded over 2010 to Hydro Ottawa in its 2012 cost-of-service application,[5] a utility that also had a decrease in OM&A expenses relative to its 2008 Board approved amount for a number of years during the IRM term. In SEC's view the similar spending pattern for the two utilities suggests that a similar overall response from the Board may be appropriate.

2.2 ***Specific Areas of Concern***

2.2.1 SEC submits there are three primary areas of concern regarding the Applicant's OM&A expenses: tree trimming, employee additions and Account 5630. It should be noted that intervenors had a difficult time comparing OM&A expenses over time since there has been significant reallocation of expenses between USofA accounts.[6]

2.2.2 ***Tree Trimming.*** The Applicant is seeking an increase $250,000 in the Test Year for expenses for tree trimming. This amount is a significant increase over past expenditures in this area. In the non-confidential description of a report commissioned by the Applicant, HHHI states that its line clearance program has been underfunded for a number of years, and there are encroachment issues prevalent throughout their system.

[3] Tr:1:67
[4] Tr:1:77
[5] Decision with Reasons, dated December 28, 2012 at 13.
[6] Tr1:1:71-72, 77

2.2.3 Tree trimming is a regular utility practice that should not see big swings in activity. Mr. Skidmore stated that the utility has has been maintaining all standard utility practices[7]. This is not consistent with a report which states that the tree trimming budget has been significantly under-funded.[8] SEC therefore submits that this budget increase has not been justified by the evidence.

2.2.4 In the alternative, f the Board agrees with the conclusions set out in the confidential report prepared by a third-party, then in our submission the Applicant's shareholder should bear the component of the cost that represents making up for past under-spending. Ratepayers should not be required to pay for the incremental tree trimming expenses necessary to remedy under-spending during the IRM term in this area, while the Applicant's shareholder benefited from that same under-spending. It is inconsistent with the IRM concept to allow a utility to defer spending during IRM, and then catch up during a rebasing year. This artificially inflates profits during IRM at the later expense of the ratepayers, and undermines the entire purpose of the mechanism.

2.2.5 ***Employee Additions***. The Applicant is seeking an addition of 7 employees since 2010 (a 16% increase), including 4 in the Test Year.[9] SEC submits that the Applicant has not justified the need for all of these additional positions.

2.2.6 As an example, there is no evidence that justifies the addition of an Engineering Technician for the Test Year due to new FIT/microFIT installations. The Applicant states only that there is a *potential* for an increase in microFIT connections from the Bridge Year's 16.[10] SEC submits that does not justify an additional fully burdened FTE. If the connections do increase to a level where current staff cannot meet the demand, then the Applicant should seek temporary help by way of third-party contractors. We note that the danger of a surge of FIT/microFIT applications may have been reduced by recent government announcements of changes to those programs.[11]

2.2.7 ***Account 5630 'Outside Services Employed'***. When questioned during the oral hearing on the increase in this account in the Test Year, Mr. Smelsky stated that it was reflecting in part, "actuarial costs for our post-employment calculations".[12] SEC submits that while that activity itself may be prudent, it is a one-time expense and should be amortized over the IRM term. We also note that there is currently no

[7] Tr:1:77
[8] Attachment to the Letter to the Board dated March 12th, 2012.
[9] Ex.4/2/6

evidence on the record as to the specific amount of the increase related to this activity. Absent evidence of the other amounts making up this increase, SEC submits that there should be an adjustment to amortize the entire increase in Account 5630 over the IRM term.

[10] VECC #IR 15(a)
[11] See *Ontario's Feed-in Tariff Program Two-Year Review Report* released March 22, 2012 http://www.energy.gov.on.ca/docs/en/FIT-Review-Report.pdf
[12] Tr:1:76

3 GREEN ENERGY INITIATIVE

3.1 *Green Energy Initiative*

3.1.1 The Applicant proposes to invest $1.4 million of capital spending in its Green Energy Initiative, the installation on 1400 of its poles, solar panels with smart grid technology. Since this project does not have a positive net present value, it would appear to us to be a pilot project. While the Applicant does reference similar technology being deployed by PSE&F in New Jersey, and Festival Hydro and Oakville Hydro in Ontario, there is insufficient information from those projects for the Board to conclude that the non-economic benefits of the Initiative outweigh the economic cost to ratepayers.

3.1.2 For a pilot project, it is submitted that the project size is too large, and installing solar panels on 10% of the poles (140) would be a more reasonable size. At the Applicant's next cost-of-service hearing, the Board and all parties will be in a better position to determine to what extent this Initiative should be expanded, if at all.

3.2 *Tax Treatment*

3.2.1 SEC has reviewed the Final Argument of Energy Probe with regards to Capital Cost Allowance ("CCA") treatment of the Applicant's Green Energy Initiative for PILS purposes. SEC agrees with Energy Probe's detailed submissions on this point.

3.3 *Related OM&A*

3.3.1 As outlined the Partial Settlement Agreement, if the Board decides not to approve the Initiative than there will need to be a corresponding OM&A reduction.[13]

[13] Partial Settlement Agreement at 12

4 PP&E ACCOUNT

4.1 *Amount*

4.1.1 The Applicant originally stated that its PP&E Deferral Account Balance is a credit owing to ratepayers of $1,462,823 and then a day before the oral hearing revised that number downward to $836,717.

4.1.2 SEC relies on the submissions of Energy Probe in its Final Argument, specifically with regards to the depreciation calculations relating to the 2011 adjustments from CGAAP to IFRS. There are a number of questions identified by Energy Probe which the Applicant will need to address in its Reply Argument to satisfy the Board that calculations are correct.

4.2 *Amortization Period*

4.2.1 The Applicant is seeking to amortize the PP&E deferral account over 20 years (March 21 Letter). SEC believes that a 20-year amortization period is inappropriate, and the correct period should be no more than the length of the IRM term, 4 years. The Applicant has raised three reasons for why a 20-year amortization period is appropriate, all of which SEC submits should be rejected.

4.2.2 First, the Applicant believes that for the purpose of intergenerational equity, a 20-year amortization period is better compared to a shorter period. Because of the transition from CGAAP to IFRS, ratepayers in the future will be paying the increase in rates associated with this change; they should see some of the benefit from this account longer-term over the full life of the assets.

4.2.3 SEC disagrees. The Applicant's argument is itself contradictory to the Applicant's proposal for disposition of the Smart Meter Rate Rider, which the Applicant seeks to collect over four years, and not over the life of that asset.

4.2.4 Perhaps more important, the concern is that customers will not be customers of the Applicant in 20 years. They should be able to receive the full benefit of the account balanceas soon as possible. Under the new accounting regime, this represents a past overcollection of depreciation from ratepayers, which due to revaluation will be added back into rate base and collected instead on the correct timeframe. Overcollections by

utilities, including ones arising out of accounting changes, should be refunded as soon as possible.

The Applicant in its updated filing provided net present value calculations of the proposal and a 4-year amortization.[14] The results clearly show that ratepayers are worse-off under the Applicant's proposal.

4.2.5 Second, the Applicant states that for reasons of minimizing rate volatility a 20-year amortization period is preferable. SEC disagrees. When taken in conjunction with the Applicant's other deferral and variance accounts, the Smart Meter Rate Rider disposition, and the cost of Stranded Meters, there is in fact less volatility, and more rate smoothness, for ratepayers with a four year amortization period.

4.2.6 Lastly, the Applicant states in its March 12th letter that shorter period amortization period will create a significant cash flow impact. SEC notes that in its Argument-in-Chief, the Applicant seems no longer to be relying on this rationale for the 20-year amortization period. This is understandable, considering the cash flow impact is only $261,056 a year and for a utility of the Applicant's size is not quite manageable.

4.2.7 The Board has not approved an amortization period on a credit or debit for the PP&E deferral account of more than 4 years, with many one or two years. It should not do so in this case, but should instead order an amortization period of the length of the IRM term, 4 years.

[14] Letter to the Board dated March 21, 2012

5 LONG TERM DEBT

5.1 *Long-Term Debt*

5.1.1 SEC has reviewed the Final Argument of Energy Probe and agrees with its extensive and detailed analysis of the Applicant's proposed long-term debt rate. SEC agrees with Energy Probe that the correct rate should be 3.85%.

5.1.2 SEC wishes to emphasis one area of significant concern, that of the Applicant's burden in this proceeding with regards to long-term debt. *The Report of the Board on the Cost of Capital for Ontario's Regulated Utilities* stated:

> The Board wishes to reiterate that the onus is on the distributor that is making an application for rates to document the actual amount and cost of embedded long-term debt and, in a forward test year, forecast the amount and cost of new long-term debt to be obtained during the test year to support the reasonableness of the respective debt rates and terms.[15]

5.1.3 In this proceeding, the Applicant has not forecast all of its expected debt for the Test Year. It did not forecast the borrowing of $5 million to finance its 2012 capital expenditures, nor it did it forecast how it intends to replace its 1 year loan from TD of $3.95 million. SEC submits that when an Applicant does not properly forecast in its evidence its Test Year debt, it cannot then use that failure as its justification to apply for the Board's deemed rate for its new financing, as requested in Argument-in-Chief.[16]

[15] *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities, (EB-2009-0084)* dated December 11. 2009 at 52-53.
[16] Argument-in-Chief at para 32.

6 OTHER MATTERS

6.1 *Costs*

6.1.1 SEC hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that the School Energy Coalition has participated responsibly in all aspects of the process, in a manner designed to assist the Board as efficiently as possible.

All of which is respectfully submitted this 13th day of April, 2012

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