EB-2012-0033

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sch.B, as amended;

AND IN THE MATTER OF an Application by Enersource Hydro Mississauga Inc. pursuant to the *Ontario Energy Board Act* for an Order or Orders approving just and reasonable rates for the distribution of electricity commencing January 1, 2013

FINAL ARGUMENT
ON BEHALF OF THE
SCHOOL ENERGY COALITION

September 23 , 2012

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0 INTRODUCTION AND SUMMARY

0.1 *Introduction*

0.1.1 On April 27, 2012 Enersource Hydro Mississauga Inc. filed an Application for new distribution rates, effective January 1, 2013 and January 1, 2014. The process included extensive interrogatories, a technical conference, an unsuccessful ADR, and a detailed oral hearing over four days.

0.1.2 This is the Final Argument of the School Energy Coalition.

0.1.3 The ratepayer groups who intervened in this proceeding have followed their normal practice of working together throughout the hearing to avoid duplication, including discussing issues, where arguments will be oral, and, where arguments will be written, exchanging drafts or partial drafts of their final arguments. We have been assisted in preparing this Final Argument by that co-operation amongst parties. Where we are in agreement with the submissions of other parties, we have not repeated their arguments here, but have adopted their reasoning where applicable.

0.1.4 Periodically in this Final Argument we use the term "No submissions". This is not intended to mean that we agree with the positions of the Applicant. Rather, we use that terminology either where an issue has little material impact on the members of SEC, or where we are confident that other parties will canvass all of the components of the issue thoroughly.

0.1.5 We have organized our submissions under the issues in the Board-approved Issues List.

0.2 *Rate Context*

0.2.1 There has been much discussion in this proceeding as to whether, or in what circumstances and what ways, it is fair and reasonable to compare the Applicant to other LDCs. Through this Final Argument we make reference to various types of comparisons, both to other LDCs and to the Applicant in prior years. Some of those comparisons will be challenged by the Applicant, either because a) they fail to consider all components of costs, or b) the Applicant has unique circumstances that make it impossible to do comparisons, or c) the Applicant has provided a bottom-up analysis and that should have priority over any objective standards.

0.2.2 Of course, the Board sets just and reasonable rates, and the analysis of costs is in reality only a step in that process. Thus, it is at least arguable that the primary way by which any LDC should be measured objectively (i.e. the primary "reasonableness" test) should be at the rates level. This is, in fact, consistent with the oft-repeated statement of the Applicant's witnesses that they should only be compared based on total costs, not any part of their costs. In a cost of service environment, rates are the embodiment of total costs.

0.2.3 The following table, taken from the rate orders for each of the Applicant's closest peers for 2012, shows the 2012 monthly bills for typical customers in each of the four main rate classes. This table is a subset of the table attached to Ex. I, Issue 2.1, SEC #23 (most easily accessed at Ex. K1.5, p. 27-28).

Rate Comparison - 2012

	Residential 800 kwhr.	GS < 50 2000 kwhr.	GS > 50 250 KW	Large User 10 MW	Customers
Enersource	$21.39	$63.13	$1,120.96	$43,081.90	192,960
EnWin	$26.85	$57.99	$1,264.39	$29,647.46	84,866
Horizon	$25.97	$49.15	$806.44	$36,209.42	234,464
Hydro One Brampton	$21.27	$48.95	$717.85	$25,889.14	134,228
Hydro Ottawa	$27.40	$56.51	$1,110.61	$46,576.82	300,664
Kitchener-Wilmot	$23.45	$50.14	$1,244.09	$28,130.67	86,611
London	$24.16	$47.98	$698.29	$43,430.79	146,974
Powerstream	$22.79	$51.84	$960.35	$12,657.63	325,540
Veridian	$23.74	$47.81	$898.45	$25,081.42	112,569
Averages	**$24.11**	**$52.61**	**$980.16**	**$32,300.58**	**179,875**
Enersource 2013	$25.91	$69.48	$1,242.83	$43,528.10	
Increase	21.13%	10.06%	10.87%	1.04%	

0.2.4 What this table shows, it is submitted, is that the Applicant currently bills its typical Residential customers less per month than most of its peers (except for its closest and most comparable peer, Hydro One Brampton), and less than the average of its peers. On the other hand, it bills its typical customers in each of the other classes more than most of its peers, and significantly more than the average of its peers.

0.2.5 So, for example, the Enersource residential bill is about 11.3% below the average of its peers. However, the Applicant currently bills its typical small GS customer about 20.0% more than the average of its peers, and the highest of its peer group. It bills a typical larger GS customer about 14.4% more than the average of its peers, third highest of the group. Compared to its closest peer, Hydro One Brampton, it charges 36.0% more. For Large Users, where admittedly the comparison is more difficult because the customers are often so unique (that is, there is an obvious question of who is "typical"), the Enersource bill is 33.4% higher than the average, again third highest out of the nine in the group.

0.2.6 Interestingly, the Applicant compares unfavourably in all four of these rate classes to Hydro One Brampton, its immediate neighbour and a utility with similar size, development history, and demographics (although, of course, some differences as well).

0.2.7 By themselves, these comparisons are not shocking. While one would expect that Enersource, with a relatively modern system and a recently-developed urban area, would have relatively low costs (like Brampton), the fact that Enersource is well above most of its peers is cause to look closely, but not cause for alarm. Having recently looked at the Toronto Hydro comparisons, Enersource in contrast looks comparatively benign. This is not a utility "run amok". It is a utility at the high end of the rate range.

0.2.8 However, implicit in this Application is the premise by Enersource that their rates are too low, and it is time for them to "catch up". What is being proposed for 2013 (shown at the bottom of the above table) is a sharp jump in those rates, such that, for example, the Applicant's residential bill would be higher, not lower, than the average of its peers (after rate adjustments for the other eight for 2013, Enersource would probably end up third highest). For the small and large GS classes, Enersource would go to 32.1% and 26.8% above the average, respectively.

0.2.9 There are two aspects of this reality that will be themes throughout this Final Argument:

(a) ***A Special Burden.*** First, when a utility wants to become an outlier, or more of an outlier, in what it charges to customers, the "just and reasonable" mandate of the Board requires that the Board apply a closer scrutiny to those proposed rates. In effect, the Applicant has a special burden (not higher, just different) to show why it is just and reasonable that it should move in that direction. This is not a legal burden, but a practical one. The Board can only meet its rate-setting responsibility if it has sufficient evidence from the Applicant of the reasonableness of its existing and/or proposed "outlier" status.

(b) ***Management Mind-Set.*** Second, in our submission management of a well-run utility should be vigilant in testing its plans and budgets against objective standards. Whatever the practices ten or twenty years ago, it is submitted that this is "best practices" today. This would necessarily involve diligently running down the reasons why it is, or is proposing to become, a rate outlier. The fact that management of the Applicant rejects completely all objective benchmarking of their costs, or even comparisons for diagnostic purposes, is a very serious cause for alarm.

0.3 ***Summary of Submissions***

0.3.1 This Final Argument contains an analysis of some of the issues arising in this proceeding. The following are the main recommendations resulting from that analysis.

0.3.2 ***2014 Rates***. SEC submits that, for detailed reasons provided in this Final Argument, the Board should not in this proceeding set rates for 2014 or beyond.

0.3.3 ***Building.*** Our analysis indicates that the Applicant is planning for 50,000 square feet of excess office space in the Test Year. At the market rents and operating costs provided by the Applicant, the total lease revenue on this space should be $1,825,000 annually. SEC believes the Board should impute lease revenue of this amount for the Test Year.

0.3.4 ***Load and Customer Forecasts***. We adopt the submissions of Energy Probe and VECC.

0.3.5 ***OM&A Budget.*** The Applicant compares unfavourably on OM&A to its peers, and also is proposing cumulative increases since 2008 far in excess of reasonable levels. SEC thus proposes a reduction in the OM&A budget of $12.2 million, representing compound annual increases in OM&A from 2008 Actual to 2013 Proposed of 5% per year.

0.3.6 ***PP&E Deferral Account***. SEC proposes that this account be cleared over four years in the standard manner approved by the Board in all other cases.

1 GENERAL

1.1 *Two Year Proposal*

1.1.1 We have been provided with a draft of the submissions of Energy Probe on Issue 1.1, and we adopt them in their entirety. There would appear to be no legitimate reason why the proposal for 2014 should be approved, and in our view the Energy Probe submissions demonstrate that this is the case.

1.1.2 SEC would like to stress five points relating to this issue.

1.1.3 ***3GIRM Option.*** It is, frankly, very surprising that the Applicant says it did not even consider whether they could accept rates for 2014 based on 3rd Generation IRM**.** The Board will have seen the questioning by SEC and others on this point in the Technical Conference, and it arose again in the oral hearing.

1.1.4 It would appear to us that, where the Board develops and promulgates a regulatory policy, it is inappropriate for a utility to simply ignore that policy altogether. Certainly, policies are not binding, and utilities are at liberty to demonstrate to the Board that, in their particular circumstances, a different approach is more appropriate. However, this still involves comparing the results of the Board's policy with the alternative approach being proposed. To simply treat the Board's policy as if it didn't exist is, at the very least, disrespectful of the Board and its processes, and should not be tolerated.

1.1.5 ***Total Cost.*** The structure of the Applicant's proposal is the separation of capital costs from OM&A costs in rates. Throughout the proceeding, the Board was reminded time and time again that Enersource manages based on total cost, and splitting between capital and operating costs is not how they run their business.

1.1.6 It is therefore inconsistent that the Applicant would seek to set rates based on a separation of the two components. In doing so, they implicitly argue that separate budgeting is appropriate, exactly the opposite of their actual operational budgeting approach.

1.1.7 ***"Layaway Plan"***. The argument that the newly-created ICR concept is necessary to avoid a step increase in a future rebasing year is disingenuous. There are circumstances, of course, where some form of rate adder is appropriate to avoid a future lumpy rate increase, and to fund utility expenditures. Smart meters was an example of that. Routine capital spending is not such an example.

1.1.8 The essence of IRM is the "total cost" concept, in which the utility manages their total costs over time, much as the Applicant says they do today. This is not something for which the utility needs total funding. What it needs is fiscal discipline.

1.1.9 Further, the ratepayers have not asked for this cash flow protection, and it would be surprising if, in a survey, they said they wanted to pay in advance.

1.1.10 Thus, it appears to us that this argument is wrong on two counts. First, the utility should be managing so that there is no step increase at rebasing. Second, the ratepayers don't need the utility to do them any favours by asking for payment in advance for a future increase that shouldn't be happening anyway.

1.1.11 ***Pilot Project.*** On a number of occasions the Applicant's witnesses promoted the value of this plan as a method by which the Board could learn about the impacts of separating capital and operating costs.

1.1.12 Aside from the incongruity of a "total cost" utility being the testbed for separation of capital and operating costs, we see no evidence that the Board needs a pilot project of this type to "learn" about the best ways to set rates.

1.1.13 ***Renewed Regulatory Framework.*** That leads to the fifth point, the recently announced Renewed Regulatory Framework for Electricity. While the Applicant has been pursuing its ICR concept in this proceeding, the Board has been busy carrying out a detailed review of its regulatory mechanisms for electricity distributors. In the week of September 10th the outline of that new system was announced, and a Board Policy setting out the details is expected to be made public in the next couple of weeks.

1.1.14 In our submission, it is within the RRFE process that changes to the structural framework should be, and have been, considered. Starting in 2014, there will be a new framework, including transitional guidelines that will apply to the Applicant as well as other LDCs.

1.1.15 There are many reasons internal to the ICR proposal that require its rejection by this Board, but at the broader level it would seem to us inappropriate for a single Board panel to approve a new rate-setting paradigm at exactly the same time as the Board as a whole has just considered and decided upon different rate-setting paradigms. The message to the distribution sector would inevitably be that, notwithstanding all the time and effort put into the RRFE, it is irrelevant before it has even been implemented.

1.1.16 For the above reasons, and the reasons set out by Energy Probe, SEC believes that the ICR proposal should be rejected, and rates in this proceeding should be set only for 2013.

1.2 ***Rates for 2015 and 2016***

1.2.1 It follows from our submissions on Issue 1.1 that, in our view, the issue of rate-setting for 2015 and 2016 should no longer be a live issue in this proceeding. Prima facie, the Applicant would be on 3rd Generation IRM in 2014, 2015, and 2016, and to the extent that it wants incremental capital in rates, it would be able to apply in those years for rate treatment under the Incremental Capital Module. When the RRFE transitional provisions are decided, those provisions may alter the rate-setting regime for the Applicant in any of those three years.

1.2.2 Thus, it is submitted that if the Board does not approve 2014 rates in this proceeding, it does not need to deal with Issue 1.2. However, in our submission it would be useful for the Board to make clear that the reason why the Board is not dealing with the issue is that there are policies in place to deal with rate-setting for those years - IRM subject to transitional rules – and therefore no further action by this Board panel is required. This would be useful to avoid any ambiguity in the future.

1.3 ***Response to Prior Board Directions***

1.3.1 No submissions.

1.4 ***Service Quality***

1.4.1 The Applicant has provided evidence showing excellent average service quality on almost every metric. They should be congratulated for that performance, whether it is measured in absolute terms or relative to their peers.

1.4.2 On a general level, it would appear to us that the only question here is whether incremental spending to improve service quality is approaching the level of diminishing returns. While we would in no way suggest that the Applicant should decrease its emphasis on service quality, that does not imply that reliability-related spending should continue to be increased without any limits.

1.4.3 In considering the spending proposals in this Application, in our submission the Board should be cognizant of the fact that the Applicant does not need spending increases to "catch up" to appropriate service quality levels. The Applicant is already at those levels, and spending on a "business as usual" basis appears to be indicated.

1.5 ***Rate and Fiscal Year Alignment***

1.5.1 SEC has consistently supported the alignment of rate year with fiscal year by electricity distributors. We see this as a fairness issue, as long as the Application to implement this alignment is filed with the Board in a timely fashion. It is submitted, that the Applicant has done so, and therefore fairness requires that the Applicant have new rates commencing January 1st, the same as their test year and fiscal year.

2 RATE BASE

2.1 *Rate Base and Capital Expenditures*

2.1.1 In this area, SEC will limit its submissions to three areas: a) customer contributions, b) overall capital expenditure levels, and c) the new head office building.

2.1.2 ***Customer Contributions***. We have reviewed a draft of the submissions of Energy Probe on this issue. We agree with those submissions, including the adjustments proposed.

2.1.3 ***Capital Expenditure Levels Generally***. SEC is concerned that the Applicant may not be reinvesting in its infrastructure at sufficient levels to be sustainable. While reliability indicators still show very good performance, other indicators suggest that a pattern of underinvestment during past years may become a problem.

2.1.4 There are two key pieces of evidence that suggest this problem. First, in Ex. I, Issue 2.1, SEC #23, the Applicant admits that their PP&E per customer from 2005 to 2010 only increased a total of 3.8%, which appears to be a very low level given that inflation over those five years was almost 10%.

2.1.5 Further, in that same IR response the Applicant notes that PP&E per customer from 2010 to 2013 increases a total of 11.3%, which seems a more reasonable level. However, if the spending on the new head office is backed out of that calculation, the increase is only 7.1%, about equal to inflation for that period.

2.1.6 Second, the 2011 Yearbook data has just been released. It shows that 2011 capital additions by Enersource were 142.3% of their depreciation, compared with 185.2% for all LDCs and 243.7% as the weighted average across the industry. Of the eight other utilities we included in their logical peer group in Section 0.2 of this Final Argument, only EnWin had a lower reinvestment rate than the Applicant. All of the rest were higher, and most were substantially higher. Similar patterns can be seen in prior years.

2.1.7 Based on this analysis, SEC does not believe that reductions to the capital budget of the Applicant are necessary (subject to our comments on the head office building, below). If anything, this would indicate that additional spending in the future may be appropriate, although without a more detailed analysis it is impossible to reach any reasonable conclusions on whether that indicator is correct, and if so how much, and when.

2.1.8 Given our analysis of OM&A spending later in this Final Argument, it also suggests that the Applicant may have too much emphasis on OM&A spending, and not enough on capital renewal. It also reinforces our view that management of Enersource would benefit from an increased use of benchmarking and objective analysis in looking at its spending decisions.

2.1.9 SEC does not believe that the evidence we are pointing to is sufficient for the Board to take any concrete action on this issue. However, in our view it may be useful for the Board to provide some guidance to the Applicant in this area, in particular with respect to the need to investigate its capital spending patterns going forward in light of industry best practices.

2.1.10 ***Head Office Building***. The Applicant houses its head office personnel in an office building at 3240 Mavis Road that is – everyone appears to agree on this – no longer suitable for their needs. It has therefore acquired an existing building – 2185 Derry Road – and proposes to move some of its head office personnel to that facility after it is refitted for their use.

2.1.11 The two buildings are not closely situated. Mavis Road is near Dundas Street, while the new Derry Road facility is 13.2 km. away, north of Highway 401. The choice of a location far from the Mavis operations centre was intentional, and was based in large part on ease of access for employees driving to work [I/2.1/Staff 12/1, p.95].

2.1.12 The Mavis Road facility is about 150,000 square feet, of which 70,000 is designed, built and used as office space [Tr.1:57]. About 250 employees work in that office space [Tr. 1:59].

2.1.13 Mavis was not originally built to house that many people. When it was originally built in 1963, it had a two storey office building as part of the original design. In 1979 a three storey office addition was constructed at the north end of the existing office space. In 1991 a further three storey office addition was constructed at the south end of the original office space. Both additions are, essentially, separate buildings with inconvenient access (through stairwells) to the original building in the centre [see Ex. I, Issue 2.1, Staff #12, Attachment 1, pages 3-5 for this information]. The total office street in the three office buildings is 70,000 square feet.

2.1.14 The Applicant engaged in the normal process of assessing the best way to expand its space. It considered building on the Mavis Road property, buying new land and building something new, purchasing an existing building, and leasing space. It did a cost analysis that compared the options. Building on the Mavis site was quickly rejected, because of traffic access and other problems [I/2.1/Staff12/1, p. 5]. Locations for acquisition of new or existing buildings were identified. Leasing was ruled out as too expensive [Tech. Tr.1:81-82].

2.1.15 In addition, a process was developed to assess how big a space would be needed. This was described as an “iterative process”, in which the Applicant’s key executives provided input to the space planner on what they wanted to see in their new building.

2.1.16 Ultimately, 2185 Derry Road was purchased this year, and is being fitted (all interior improvements had been removed by the previous owner) for a 2013 move-in date.

2.1.17 ***Evidence of Mr. Kingdon.*** The Applicant retained TAC Facilities Group to do space planning. Mr. Pastoric described them, and their work, as follows [Tr.1:60]:

> *"Going back to our TAC Facilities Group, who are experts in sizing buildings, they've indicated that the building that we're occupying in Derry is just slightly less than their calculations of industry standards. So, moving the 150 employees up to the new building is just moving it to, essentially, industry standards."*

2.1.18 It turned out this was wrong on many levels.

2.1.19 First, when Mr. Kingdon from TAC Facilities Group appeared as a witness, the Applicant declined a request to qualify him as an expert [Tr.4:3-4], despite his having been referred to as an expert by Mr. Pastoric more than once [see also Tr. 1:21; Tr. 2:30, etc.].

2.1.20 The rules of evidence before the Board on this point are fairly well-known. Utility witnesses give evidence on behalf of their employer, and while their experience and knowledge are taken into account, they are not primarily giving opinion evidence. They are, instead, giving evidence on what they actually did, and why.

2.1.21 Individuals who do not work for the utilities are sometimes brought in to give evidence, usually because they had a specific expertise that was unavailable at the utility. They give evidence on the work they did, and their expertise informs the Board as to the value of their results or conclusions. The Board has a series of rules to qualify experts, including a kind of *voir dire* at the outset before the person is accepted as an expert witness.

2.1.22 In this case, in addition to referring to TAC as experts, the Applicant has asked them, in direct examination, to give evidence on the reasonableness or appropriateness of the results of their work [e.g. Tr. 4:7, and many other places]. Further, in response to cross-examination, Mr. Kingdon on numerous occasions provided his "opinion" on what was reasonable, normal or appropriate.

2.1.23 In general, individuals who are not qualified as experts are not in a position to give opinion evidence that would require a special expertise. They can tell the Board what they did, e.g. "I prepared this spreadsheet using a proprietary space planning model". They can express opinions on matters that don't require a special expertise, e.g. "In my opinion the Blue Jays need a better closer." What they are not permitted to do is provide opinions on matters requiring a special expertise.

2.1.24 For this reason, and the others set out below, SEC believes that the Board should give no weight to the statements by the Applicant that they relied on expert space planners, and should give no weight to any statements by Mr. Kingdon that express an opinion on the appropriateness of the space plan of Enersource.

2.1.25 Second, Mr. Kingdon clearly denied that he gave any opinion on "industry standards", and in fact doubted that there were any [Tr.4:49]. Mr. Pastoric's repeated references to their "expert opinion" on industry standards [see, e.g. Tr.2:34] appear to be simply exaggerations.

2.1.26 Third, the implication that TAC "sized" the building requirements is, at best, misleading. In fact, TAC engaged in an "iterative process" in which Enersource basically told them what they wanted, and they laid out floor space accordingly.

2.1.27 For example, TAC did not tell Enersource how many meeting rooms they needed. In this process, the Applicant effectively told TAC how many they wanted, and they designed with that in mind [Tr. 4:38]. There are numerous references of this kind throughout the evidence.

2.1.28 The result of this analysis is that the Board is left without any evidence from the Applicant on whether the office space they will have – and they propose the ratepayers fund – in the Test Year is appropriate. They have provided evidence that their current space is inadequate [Tr.1:18-20], which is not disputed. They have also provided evidence on how much they want for the future. At the same time, they have denied that they have any expertise to assess their own space needs [Tr. 2:36], and they have not provided any useable third party evidence of the appropriateness of the space they want. They had ample opportunity to do so.

2.1.29 It is submitted that, prima facie, the Applicant has not justified the space requirements it is proposing. The Board is therefore forced to do its own review, and reach conclusions on what space requirements look reasonable to the Board based on the limited information available to it.

2.1.30 ***Basic Facts.*** What we know is that the Applicant proposes to move 150 people currently housed at Mavis, to the new Derry Road facility, where there would have a total of 79,000 square feet [Tr.2:59-60]. This works out to an average of 527 square feet per employee. We also know that 100 employees would be left at Mavis Road, with 70,000 square feet of office space available to them.

2.1.31 There appeared to be some confusion as to the numbers of employees. The summary of the space design (which did not specifically contemplate Derry Road at the time, but has been offered as the basis for the plan) is at Ex. I/2.1/Staff #12/1, p. 101-102.

As subsequently corrected for an addition error in the underlying spreadsheet, the plan shows 176 people at Derry, and 127 people at Mavis, at the move-in date. This 303 total is substantially in excess of their current 250 employees using offices [based on 143 outside employees out of 391 total employees, the actual figure would be 248 – see Tr. 1:56 and the 2-K for these figures]. After five years, these totals are expected to increase to 189 and 134, for a total of 323. This implies a more than 30% increase in office personnel over five years based on current actuals. This is clearly not credible.

2.1.32 It is submitted that there is no actual confusion over the number of employees needing office space. Assuming the complement for the Test Year is the full 391 set out in the 2-K, there will be 143 outside employees and 248 inside employees. They will have 149,000 square feet of office space available to them, in two locations. The resulting ratio of employees requiring office space to available space is just over 600 square feet per employee.

2.1.33 ***Industry Standards.*** The Applicant was unable to provide any information on industry standards, but Mr. Kingdon did admit that there are standards that are used, including those from the U.S. General Service Administration, and the Workplace 2.0 standard of the Canadian Federal Government (PWGSC) [Tr.4:50-51].

2.1.34 It is public knowledge that the cap for the Workplace 2.0 standard is 193 square feet per employee, and that the cap for the US GSA is 230 square feet per employee. It is submitted that these external figures, used by credible organizations, should inform the Board's assessment of whether the Applicant's proposals are in a reasonable range.

2.1.35 In this respect, we note that it was open to the Applicant to provide its own evidence on industry standards, and how they met those standards. Indeed, given their onus to prove their case, it was likely their responsibility to do so. They have failed to do so, and the Board must use the best evidence it has available to it.

2.1.36 ***Specific Elements of the Plan.*** In addition to looking at the space requirements on a global basis, it is appropriate to look at the individual elements of the space proposal to see whether they appear reasonable.

2.1.37 We will not go through the proposal in detail. A cross-examination was conducted with respect to Ex. I/2.1/Staff #21/Attach1 and K.3 and K.4, which are summaries of that attachment. A number of specifics were addressed [see Tr. 4:29-46]. Some of the questions that should be raised are the following:

(a) Executive Boardroom at 1000 square feet, i.e. about 20 x 50.

(b) In addition to a large office for the CEO (380 square feet), there is an equally large office proposed for the Chairman, who does not have an office now and does not work full-time for the Applicant.

(c) The provision of three large meeting rooms, total 3750 square feet, so that the company can have meetings with all 391 staff. The Applicant claims this may happen a dozen or more times a year. SEC believes that is not reasonable. The size is necessary, says Mr. Kingdon, because in those meetings the room may need to be set up classroom style so that people have a desk in front of them. It is submitted this is also not credible.

(d) A total of 32 meeting rooms for 248 staff, including a number of dedicated meeting rooms. There are, in addition, work rooms and other dedicated spaces, plus individual offices sized to allow for meetings. One small group of three people, for example, has their own dedicated meeting room of 400 square feet.

(e) The overall space plan provides for actual offices or workspaces for 299 people totaling 27,348 square feet, or about 91.5 square feet per person on average. It also provides for 81,439 square feet of non-dedicated space, which is common areas (including common areas dedicated to particular groups), circulation, building elements, etc. This is another 272.4 square feet per person. In both cases, the per person elements are understated, because as noted above the number of people actually using the space will be 248.

(f) The CEO's office, including Chair, EVP and support staff, is planned [p. 142 of Attachment 1] to comprise 4647 square feet.

(g) The lobby and customer service areas are planned to take up 5,676 square feet at Derry, plus there will be some customer service areas (undetermined as yet) at Mavis. This appears to us to be at least double, and perhaps triple, the size of the lobby and customer service areas at larger utilities like Enbridge.

(h) There are 10 printer/fax stations at Derry, each about 15 x 20, total 3,000 square feet. No evidence was provided as to why the printer/fax stations would be so large, and why the employees would need one of that size for every 15 employees.

2.1.38 There are many other examples, as a review of the space breakdowns will show. It is submitted that these are indicative of planning for excessive space "needs"**.**

2.1.39 ***The Applicant's Justification Based on Cost and Comparison to Powerstream.*** Faced with the suggestion that the Powerstream Head Office is designed to house 250 employees in 92,000 square feet, the Applicant produced its own comparison, K4.6. In this comparison, the Applicant admits to planning to "need" about 15% more square feet per employee, but says that its costs are lower so its cost per employee is better.

2.1.40 The Applicant's comparison is flawed in three respects.

2.1.41 First, it does not compare move-in numbers. Powerstream moved 250 employees into 92,000 square feet, not 270 as Enersource suggests. The actual was 368 square feet per employee. Similarly, Enersource is moving 150 people, not 202, into 79,000 square feet. The actual is 527 square feet per employee, which is 43.2% more than Powerstream.

2.1.42 Second, K4.6 just compares Derry to the new Powerstream Head Office, failing to mention the 100 employees left at Mavis in 70,000 square feet.

2.1.43 Third, the Applicant focuses on their 3.5% lower cost per employee, without noting that Powerstream built a new building to LEED Gold standards (thus saving on operating costs downstream), and Enersource bought a 16 year old building, which presumably will cause ratepayers to incur costs for maintenance and replacement earlier than would be the case with Powerstream.

2.1.44 In any case, of course if the correct employee numbers are used, the Enersource older less efficient building costs $133,333 per employee, which is about 20% higher than the $110,800 per employee for the Powerstream building.

2.1.45 Thus, it is submitted that the Applicant's comparison is not helpful to the Board.

2.1.46 ***The Phantom Mavis Space.*** All of this leads to what is perhaps the most important aspect of this analysis, the fact that the space plan includes only 28,900 square feet of the 70,000 square feet of office space at Mavis.

2.1.47 Little evidence was provided on this additional 41,000 square feet. Until we asked in cross-examination, the Board had, the Company admits, nothing at all before it on this space [Tr.4:25].

2.1.48 When pressed on this, they first said it would be "meeting rooms" [Tr. 4:22], then, what that was shown to be incorrect, "locker rooms, shower rooms" and training areas [Tr. 4:23], and when that was shown to be incorrect, "a place to dry their clothes" and "warehousing" and "garage" [Tr. 4:28]. None of those are actually correct. We are dealing with an original area, and two additions, all built to be offices. They are not going to be used as warehouse space.

2.1.49 Asked specifically whether they had a plan for this space, the Applicant said they do not [Tr. 4:29]. The Board, in fact, has no credible evidence on which to determine how this just over 41,000 square feet, now used as offices, will be used.

2.1.50 ***Excess Space.*** Based on the various points above, SEC submits the Board should conclude that the Applicant, with the acquisition of the new Derry Road head office building, will have significant excess space, both in the Test Year and in the foreseeable future.

2.1.51 There are several ways to assess the amount of the excess space:

(a) The Canadian government standard, Workplace 2.0, would require about 48,000 square feet for 248 employees, including common areas. Adding a generous 30% for building features and infrastructure, plus 10% for growth, this implies that Enersource is seeking about 80,000 square feet too much.

(b) The US government standard of 230 square feet per employee would require about 57,000 square feet for 248 employees, including common areas. Adding the same 30% for building features and infrastructure, and 10% for growth, results in total office needs of about 82,000 square feet, implying that the current plan is high by 67,000 square feet.

(c) Powerstream had a move-in ratio of 368 square feet per employee, all-in, assuming the need to accommodate future growth. This ratio, applied to Enersource's 248 employees, would imply that Enersource needs just over 91,000 square feet, and thus is planning for about 58,000 square feet too much.

(d) Enersource provided a plan for about 108,600 square feet out of the 149,000 square feet available to them, assuming 303 office employees in the Test Year. This is a ratio of 358 square feet per employee. When applied to the actual number of inside employees in the Test Year, 248, this means they need just under 89,000 square feet in total (remarkably similar to the Powerstream number), meaning they are 60,000 square feet high.

(e) Enersource has provided explanations for 108,600 square feet of space, even if some of those explanations are problematic. At least 40,400 square feet is therefore unaccounted for, and no useful evidence has been provided as to how it will be used.

2.1.52 Based on this analysis, SEC believes it is reasonable for the Board to determine that the Applicant has planned for 50,000 square feet of excess space**.** That is, the maximum reasonable number of square feet the ratepayers should be paying for in rates should be roughly 100,000 square feet. In light of the Powerstream comparable (92,000 square feet for the same number of total employees, 250), we believe this figure is right at the high end of what is reasonable.

2.1.53 ***Remedy.*** On the face of it, the Board could simply disallow inclusion of 50,000 square feet of the new building in rate base, and disallow the incremental operating costs, property taxes, etc. associated with that space.

2.1.54 What this implies, however, is that the Applicant should not have purchased the Derry Road building, i.e. it was not a prudent decision. SEC is not convinced that is the case.

2.1.55 In our submission, the Applicant did take proper steps to assess whether it needed additional space, and if so what options it had to get that space. Were those steps perfect? No, clearly not. However, we agree that more space was needed, and we do not think that the purchase of Derry was an inappropriate response to that need. For example, in the longer term (20 years, for example) there could well be space needs that justify the purchase of that much additional space, and the stability available as a result of having space available for the long term may be a legitimate goal.

2.1.56 The mistake the Applicant made, in our submission, is in assuming that they had to use all the space they acquired. A more prudent decision would have been to plan their space based on the actual space available, and industry standard ratios. That would have included having a real plan for any office space at Mavis that they wanted to convert to other uses, instead of "we'll get to that later".

2.1.57 Had the Applicant taken those prudent steps, the evidence demonstrates, it is submitted, that it would have realized it had 50,000 square feet of space available to lease to third parties. It would therefore have come to this Board with a plan to lease that space (until it is needed by the utility in the future), and thus an offsetting amount of lease revenue covering the rate base and operating costs associated with the excess space.

2.1.58 It is therefore submitted that the appropriate remedy is for the Board to impute lease revenue for that excess space for the Test Year. The Applicant can, of course, retain all of the space for its own use if it wishes, but the ratepayers should not be forced to pick up the tab for that excess space.

2.1.59 In para. 3.2.2 and following of this Final Argument, SEC proposes a method of calculating that imputed rent based on the evidence before the Board in this proceeding.

2.2 ***Working Capital Allowance***

2.2.1 We have reviewed a draft of the detailed analysis of Issue 2.2 by Energy Probe, and we agree with that analysis.

2.3 ***GEA Plan***

2.3.1 No submissions.

2.4 *Capitalization Policy and Allocation Procedure*

2.4.1 SEC is concerned that once more the Applicant is proposing to reduce its overall level of capitalized costs in a cost of service year. There does not appear to be any good reason for this, and it is submitted that rates should be set based on a more business as usual approach to capitalized costs.

2.4.2 SEC notes that in 2008 the Applicant's rates were set on the basis of 25.7% of compensation being capitalized, but the actuals were 29.4% [Ex. 4/3/1, App. 2-K]. However, compensation in total went up, so the dollar impact was muted.

2.4.3 What the Applicant is now proposing is an increase in total compensation from 2010 to 2013 of about 10%, but an increase in the OM&A component of total compensation of 26% [also 2-K]. This comes about because the capitalized component would drop from 30.8% to 20.7% as proposed. This has the effect of increasing revenue requirement without increasing actual spending. When asked about this [Tr.3:62], the Applicant's witnesses did not really have a very satisfactory answer. As they have described it, their allocation is somewhat of a "black box", and this just happens to be the result it produces.

2.4.4 On this issue, we have reviewed the draft submissions of Energy Probe, which set this out in more detail. They have proposed that OM&A and capital spending be adjusted by increasing the assumed capitalized compensation from 20.7% to 26.1%. We agree with that analysis.

2.4.5 We note that this adjustment would, in our view, be subsumed within the OM&A adjustment we propose later in this Final Argument. Because our OM&A adjustment uses a top-down approach, making a further adjustment for capitalized compensation would be duplicative.

3 OPERATING REVENUE

3.1 *Load Forecast and Billing Determinants*

3.1.1 We have reviewed the analyses of Issue 3.1 by Energy Probe and VECC, and we agree with their conclusions.

3.2 *Other Revenues and Charges*

3.2.1 Other parties will consider aspects of this issue, and we will not deal with those in this Final Argument. Our submissions are limited to our proposed remedy for the excess size of the Applicant's office space, i.e. imputed rental income.

3.2.2 ***Imputed Rent.*** Earlier in these submissions SEC has concluded that the Applicant is planning for 50,000 square feet of excess office space in the Test Year. As earlier discussed, it is submitted that the appropriate way for the Board to adjust for that excess is to assume that the Applicant will lease that space to third parties, on market terms, and use those revenues to offset the incremental capital and operating costs included in revenue requirement for that space in the Test Year.

3.2.3 Market rents for space suitable for Enersource are contained in the evidence at page 4 of Exhibit I, Issue 2.1, Staff #12, Attachment 2. The figure cited by the Applicant's advisors is $23.00 per foot. At the same reference, the operating costs per foot are estimated at $13.50. These were the figures used by Enersource in its cost analysis.

3.2.4 Based on the Applicant's market cost estimates, SEC submits that the Board should impute rental income of $1,825,000 in the Test Year related to the 50,000 excess square feet of office space.

4 OPERATING COSTS

4.1 *Overall Level of OM&A*

4.1.1 SEC is aware that other parties will be providing extensive submissions with respect to OM&A levels, so in this Final Argument we will endeavour not to be duplicative of those submissions. The Board will see a more detailed analysis, both on a top-down basis, and on a line by line basis, in the Final Argument of Energy Probe, and we are aware that CCC will also be dealing with this issue fully. Subject to our comments below, we agree with the thrust of those submissions.

4.1.2 There would appear to us to be two components to the OM&A analysis. First, on an absolute basis is Enersource spending more on OM&A than other utilities? Second, is Enersource managing to keep its OM&A spending increases under control over time? We will deal with each of those in turn, and then with some more general concerns.

4.1.3 ***Relative OM&A Spending Levels***. In doing comparisons with other LDCs, SEC is relying primarily on OM&A per customer. We are aware that the Applicant thinks that is an unfair measure when comparing between LDCs, and we agree that the size of the Applicant's Large User class skews some of those comparisons. On the other hand, the metric that the Applicant prefers to use, OM&A (or total cost) per kwhr., is skewed in the other direction, and significantly more so.

4.1.4 Thus, for the purposes of a high level analysis, we are using the metric that is used by the Board already, OM&A per customer. We have tried to look at the data enough different ways that any skewing of results is minimized. However, we also note that we are not proposing that any hard conclusions be reached from OM&A per customer comparisons between LDCs. Rather, we are treating them as diagnostic, and our conclusions will be based on other metrics, below, such as increases over time at Enersource.

4.1.5 We also note that all references to the "peer group" refer to the eight utilities plus Enersource listed in our table at Section 0.2 of this Final Argument. This includes the proxy group listed in their own Shareholders Agreement, plus four others, being one larger than the proxy group, and three smaller. However, all of the general results noted below are true, at similar levels, if the proxy group subset is used instead.

4.1.6 To see if there is an overall higher level of OM&A spending at the Applicant relative to the peer group, we start with a look at the oldest numbers, OM&A per customer from 2005. The list of this information can be found in the attachment to Ex. I, Issue 2.1, SEC #23, which is page 29-30 of Ex. K1.5.

4.1.7 What we see is that in 2005, the average OM&A per customer of the peer group excluding Enersource was $164.75, and Enersource was at $229.60, or 39.4% higher. Enersource is in fact higher than all of the peers except EnWin, and higher than all of the proxy group.

4.1.8 A similar result is seen in 2010, with the peer group average at $188.76, and Enersource at $249.14, 32.0% higher. The comparative trend is favourable – 39.4% drops to 32.0% - , but the differential is still very high. (We note that this comparative trend appears to continue to be favourable in the recently-released 2011 data, i.e. with Enersource at only 26.8% above the average of the peer group, although we have not had sufficient time to review that data in detail. As is clear from the year over year Enersource comparisons below, however, this trend is obviously not continuing in 2012 and 2013.)

4.1.9 We note that the OM&A per customer comparisons are consistent with the general thrust of the bill comparisons we provided earlier in this Final Argument. That suggests that at least some of the differentials seen in OM&A per customer are reflected in an overall total cost differential as well.

4.1.10 One way to test whether this information has explanatory value is to look at key components of the OM&A data on a different basis. The biggest such component is total compensation.

4.1.11 To do this comparison, SEC took the most recent 2-K information for Enersource and compared the average total compensation per FTE with some of the peer utilities using their most recent 2-K data. (Time constraints prevented us from looking at all eight of the peers, only five, but the other three are likely lower anyway.)

Comparison of Average Compensation per FTE

LDC	*Year*	*FTEs*	*Total Comp (SW&B)*	*$ per FTE*	*Source*
Enersource	2013	391	$44,095,373	$112,776	EB-2012-0033 Ex. 4/3/1, App. 2-K
Powerstream	2013	569	$65,882,355	$115,786	EB-2012-0161 Ex. D1/5/5
Hydro Ottawa	2012	598	$59,048,944	$98,744	EB-2011-0054 Ex. D3/1/1, Attach AC
London	2009	279	$23,593,500	$84,595	EB-2008-0235 Ex. 4, p. 23
Horizon	2011	428	$41,642,494	$97,296	EB-2010-0131 Ex. 4/2/10, p. 11
Hydro One Brampton	2011	231	$21,743,896	$94,129	EB-2010-0132 Ex. 4/4/9.1

4.1.12 What this shows is that, relative to this group of peers, the Applicant has higher total compensation per employee than all but Powerstream. The Powerstream figures are, of course, proposed only, but they are also the only figures that are 2013 numbers, similar to Enersource.

4.1.13 This suggests to SEC that Enersource has overall compensation levels that are on the high side, perhaps helping to explain their relatively high OM&A per customer. For example, if Hydro Ottawa's total compensation per FTE is escalated by 3.5% from 2012 to 2013, the average for Enersource is still about 10% higher. If Hydro One Brampton is escalated at that rate for two years, Enersource is 12% higher, if Horizon has a similar escalation, Enersource is about 8% higher, and if London is escalated four years at a similar rate, Enersource remains 16% higher.

4.1.14 SEC recognizes that there could be many reasons for this, such as a different mix of employees (higher levels of management employees at Enersource for example, which we saw is their current trend [Ex. I/4.1/EP#47]), or higher pay levels, or higher benefit costs. What is undisputed is that Enersource has higher personnel costs than its peers, except Powerstream.

4.1.15 As noted earlier, SEC is not proposing that the Board use any of the above comparisons with other LDCs (including the rate comparison earlier) as a basis for reducing revenue requirement. These comparisons go to the reasonableness of the proposals of SEC (see below) and others, by demonstrating that, at least directionally, increasing control over OM&A spending is needed at this utility.

4.1.16 ***Applicant's OM&A Increases Over Time.*** Enersource witnesses said a number of times that they assess their cost performance by comparison to their own past spending [e.g. Tr. 3:83, and many other references]. SEC believes that this can assist the Board as well in determining the reasonableness of the OM&A spending proposals.

4.1.17 The Applicant has provided a breakdown of OM&A costs from 2008 to date in JT2.11. That breakdown separates what the Applicant calls normal Business Unit increases from those that it considers special cases.

4.1.18 In our submission, when a top-down analysis is being done, it is not appropriate to segregate costs and, in effect, treat them as "not counting". All costs count. There may be explanation of large increases in certain categories, which explanations justify the increases. However, step one should be to assess the increases.

4.1.19 Therefore, to have a proper starting point for an analysis of cost increases at Enersource, SEC has restated some the table in JT2.11 by including the so-called special case items in the main expense lines. Asset Management costs are part of Engineering & Operations, Smart Meter costs are part of Metering, and the incremental cost of the New Office Building is part of Facilities Management.

4.1.20 We have also used 2008 Actual figures, rather than 2008 Board approved. 2008 is the earliest year for which we have data on how much it actually costs to operate this LDC. It is therefore the appropriate base for determination of how much it should actually cost to operate the LDC in 2013. The fact that the Board may have approved a different figure for 2008 rates is not, in our view relevant when the purpose is to do an empirical analysis. The 2008 Board approved brings in other factors such as budgeting approach, regulatory success, and ADR negotiations, none of which are actually relevant to what it really costs to operate the utility. Hence, in our submission 2008 Actual is the more appropriate starting point.

4.1.21 That new table shows the following:

Comparison of OM&A Costs from 2008 to 2013

Expense Category	*2008 Actual*	*2013 Proposed*	*Increase*	*Percent*	*Compound %*
Health, Safety & Security	$597	$846	$249	41.7%	7.2%
Customer Care	$6,653	$8,975	$2,322	34.9%	6.2%
Engineering & Operations	$8,517	$15,076	$6,559	77.0%	12.1%
Metering	$662	$2,359	$1,697	256.3%	29.0%
Exec. Admin & Corp. Alloc.	$9,921	$12,574	$2,653	26.7%	4.8%
ISTS	$4,477	$8,227	$3,750	83.8%	12.9%
Reg. Affairs	$898	$1,681	$783	87.2%	13.3%
Facilities Management	$1,378	$3,045	$1,667	121.0%	17.1%
Bad Debt	$1,270	$3,550	$2,280	179.5%	22.6%
Other OM&A	$1,767	$1,904	$137	7.8%	1.5%
Totals	$36,140	$58,237	$22,097	61.1%	10.3%
IFRS Overhead Burdens	$0	$2,774			
Full Totals	$36,140	$61,011			

4.1.22 In our submission, an apples to apples comparison cannot include the changes due to IFRS. Therefore, our top-down analysis uses the line by line figures, and the "Totals" figure above.

4.1.23 The Applicant has provided explanations for some of these surprisingly high figures. Facilities Management, for example, has to increase by a compounded 17.1% per year because they have to look after two buildings instead of one. Engineering and Operations has to increase by a compounded 12.1% per year because, as they do more inspections of their equipment, they find more things they have to do. Bad Debt has to increase by <u>only</u> a compounded 22.6% per year because the Applicant spent additional funds to control this cost, without which the increase would have been more (about 28% per year compounded for five years). Some of those explanations are obviously wrong, such as the notion that metering costs should go up by 256% because the personnel who were working on the smart meter rollout now have to have something to do, and the meters are still there. This is just not credible.

4.1.24 What these individual explanations fail to deal with is the clear spending pattern shown by the table, i.e. every single area increases at a rate well in excess of any reasonable level. The lowest increase, in fact, is two and a half times the level of inflation, and is the lowest despite that fact that we know that area (Exec., Admin. and Corp. Alloc.) has its own problems due to changes in the structure of the corporate group. Other areas such as IT spending at 12.9% per year compounded, are astronomically high.

4.1.25 Other parties will propose specific adjustments to the very high OM&A proposal. We have seen some of those adjustments of particular OM&A categories, and they are generally well supported by the evidence.

4.1.26 However, our approach is to look at this from the top down. The Applicant is proposing that its OM&A increase by a compound rate of 10.3% per year for five years. By any standard, this is not a reasonable rate of increase.

4.1.27 Taking all of the explanations and other factors into account, SEC believes that the maximum annual compound increase in OM&A that could be justified for Enersource is 5% per year from the 2008 Actuals. This factors in customer growth, inflation, and unusual cost pressures. This translates to an OM&A budget for 2013, before IFRS adjustment, of $46.1 million. With the IFRS adjustment, the OM&A budget would be $48.9 million. This is a reduction of $12.2 million from the Applicant's proposed budget.

4.1.28 We note that we have also calculated the increase if the Board were to allow a 6% annual increase, compounded over five years. SEC is not proposing an increase on that scale, which we believe is too high, but notes that it would produce an OM&A budget of $51.1 million, or a $9.9 million reduction from the budget proposed by the Applicant.

4.1.29 ***Objective Budgeting***. We were struck, at many points in the process, by the Applicant's inability to see the value of applying objective tests when setting budget levels. It is one thing to be less than rigorous in assessing the reasonableness of spending proposals. It is quite another thing when the utility's management appears not to even understand the concept, or how it would be applicable to them.

4.1.30 This approach to spending decisions is manifested in a number of different but related ways:

> ***(a)*** ***Cost Benefit Analysis.*** The Applicant's management does not require, or do, cost benefit analyses for any spending proposals [Tr.3:96]. Sometimes they anticipate that there will be future cost savings, but they don't know whether they will be sufficient to justify the spending, and in any case they don't make

any attempt to quantify them. It was clear in the various discussions on this that they do not understand why or how this would be applicable to their business.

(b) ***Lack of Control.*** When discussing comparative metrics, management treated not only volumes, but much of costs, as being not within their control [Tr.3:118].

(c) ***Units of Work.*** It is common in the utility business to expect to get a certain number of units of work for given spending, but the Applicant's witnesses, in cross-examination by Mr. Faye, did not appear to understand why this would be of value [Tr.3:26-27].

(d) ***Productivity.*** Asked about what happens when productivity reduces costs to get particular items done, the Applicant's witnesses rejected completely the idea that less spending could be the result. The result, they said, is that more work gets done, not less money gets spent [Tr.2:34].

(e) ***Cost Avoidance vs. Cost Savings.*** The discussion of the difference between cost avoidance and cost savings was particularly confusing [Tr.3:85 and Tr.2:33]. It is clear that the idea a cost will actually go down – ever – is never in their minds.

(f) ***Straw Man Increases.*** In fact, they admit that they operate on a basic assumption, i.e. costs will go up in the future [Tr.3:90]. While that may be true in general, it is hardly the assumption that should drive budgeting of individual spending plans. We saw a pattern in this proceeding of "productivity" spending that did not reduce costs, but only reduced assumed (and sometimes not even quantified) future increases: bad debts, station maintenance, etc.

4.1.31 What concerns us the most is that the Applicant does not have an objective view of what they "need" to spend. When you pack your suitcase for a trip, you make a list of things you "need". When you realize that they will not all fit into the suitcase, you prioritize and, through the objective limit provided by the size of the suitcase, you re-define what you "need". We saw time and again that the Applicant and its management did not understand how the second part of this process could be applicable to utility spending.

4.1.32 Interestingly enough, in IRM years the Applicant does operate to an objective standard, but it has nothing to do with keeping rates down. The shareholders want their return, and rate levels are predetermined by formula, so there is an external need to control costs. Costs must be controlled so that the shareholders get their return. Yet, when we discussed this in cross-examination [Tr.3:77-81], the Applicant did not grasp that this control mechanism was inapplicable in a cost of service year.

4.1.33 One of the things IRM should be doing is helping former municipal utilities to make the transition to a more business-oriented approach. Where in the past budgeting was simply a matter of convincing someone how much you needed to spend (i.e. an entirely bottom-up approach), with little reference to rate impacts, LDCs today are faced with a "market", in the form of a regulator acting as a market proxy. The use of a formula to set rates, by decoupling revenues from spending proposals, should promote a more objective, top-down approach to budget analysis.

4.1.34 Unfortunately, the Board has seen that some utilities make this transition quickly and effectively, while others have more trouble with it. It appears to us that Enersource is in the latter group. However well they run the utility operationally – and all evidence indicates that they are very good on that front – they do not appear to have internalized the need to drive productivity and efficiency improvements, the need to test spending against objective standards, and the market imperative to keep their prices/rates down.

4.1.35 The Board is in a good position to assist the Applicant, providing guidance and direction so that they start to adopt best practices in this area. Both the utility and its ratepayers would benefit from increased rigour in spending decisions and productivity initiatives, and benchmarking of results to support that rigour.

4.1.36 SEC asks that the Board, in its decision on this Application, provide that guidance and direction.

4.2 ***Depreciation and Amortization***

4.2.1 No submissions.

4.3 ***Income and Other Taxes***

4.3.1 We have had the opportunity to review the submissions of Energy Probe respect to taxes, and we adopt both the analysis and the conclusions in those submissions.

4.4 ***Shared Services and Corporate Costs***

4.4.1 See our submissions under Issue 4.1, above.

5 CAPITAL STRUCTURE AND COST OF CAPITAL

5.1 *Capital Structure, ROE and Short Term Debt*

5.1.1 No submissions.

5.2 *Long Term Debt*

5.2.1 No submissions.

6 COST ALLOCATION

6.1 *Methodology*

6.1.1 See our submissions under Issue 6.2, below.

6.2 *Revenue to Cost Ratios*

6.2.1 The Applicant has proposed different revenue to cost ratios compared to those most recently approved by the Board, i.e. in EB-2007-0706.

6.2.2 Two things have happened.

6.2.3 First, the Applicant has done a new cost allocation study, based on 2013 costs and proposed rates. That shows that costs have essentially increased for some classes, and decreased for others. As a result, residential, for example, which had an approved revenue to cost ratio of 91.5% in EB-2007-0706, would in fact have a new ratio of 87% under the new cost allocation study.

6.2.4 Second, the Applicant has proposed to move each class from the level in the cost allocation study, closer to the Board-approved revenue to cost ratio.

6.2.5 In our submission, the starting point for this process should be the Board-approved revenue to cost ratios for each class. All other things being equal, rates proposed for 2013 should use revenue to cost ratios that are not further away from unity than the existing Board-approved ratios.

6.2.6 In this case, the Applicant has not done precisely that, but has gotten close. The reason, it appears, is the impacts on the classes, which can be seen graphically in the last line of the table we have provided in Section 0.2 of this Final Argument. The proposed movement would produce a 21% increase for residential, compared to 1% for Large Users, and about 11% for the two non-residential general service classes.

6.2.7 SEC believes that it would in fact be better ratemaking to move each class to the previously approved revenue to cost ratios. However, in light of the differential in impacts (which would remain even if the Board makes significant reductions to revenue requirement), SEC believes that the proposal from the Applicant is a reasonable one.

7 RATE DESIGN

7.1 ***Fixed/Variable Splits***

7.1.1 No submissions.

7.2 ***Low Voltage, USL, and <50 Merger***

7.2.1 No submissions.

7.3 ***Loss Factors***

7.3.1 No submissions

7.4 ***RTSRs***

7.4.1 No submissions

7.5 ***Tariff of Rates and Charges***

7.5.1 Subject to the changes in rates and charges that would result from the submissions made elsewhere in this Final Argument, SEC has no further comments on this issue.

8 DEFERRAL AND VARIANCE ACCOUNTS

8.1 *Balances, Allocation and Disposition*

8.1.1 Subject to our comments under Issue 9.1, SEC has no submissions.

8.2 *Rate Riders*

8.2.1 No submissions.

8.3 *New and Continued Accounts*

8.3.1 Subject to our comments under Issue 9.2, SEC has no submissions.

9 MODIFIED INTERNATIONAL REPORTING STANDARDS

9.1 *PP&E Transition*

9.1.1 SEC has no comments on the balance in the standard PP&E deferral account. However, we are concerned about the proposal to clear it over one year through a rate rider, instead of through depreciation expense over a four year period consistent with the Board's policies.

9.1.2 The proposal to clear over one year is said to be in order to soften the impact of the rate increase in this Application. In light of the submissions we have made elsewhere in this Final Argument, it is clear that SEC does not believe the large proposed rate increases can be justified based on the evidence. If the Board reduces the approved revenue requirement significantly, as many parties urge, the effect is that this mitigating clearance is no longer necessary. In fact, it could be counterproductive, since the result would be an incremental increase in bills in 2014 when the disposition is completed.

9.1.3 Use of a rate rider also does not appear to be appropriate. The Board has an established policy for how to do this, and unless there is some special reason why this change would be necessary in this case, we see no reason to diverge from the policy. Further, we note that use of a rate rider changes the amount of the rate increase under the IRM formula, so unless an additional increase is considered appropriate, some adjustment would be required to account for that as well.

9.1.4 It is at least arguable that the rate rider treatment would be necessary due to the complication of the ICR. Given our position with respect to the inappropriateness of the ICR, SEC believes that this is not a reason to depart from Board policy.

9.1.5 Therefore, it is submitted that the clearance of this account should be over four years in the normal manner, rather than through a rate rider. We have seen the return calculations by Board Staff in their Final Argument, and we agree that those adjustments, which would also be required, are calculated correctly.

9.2 *MIFRS Deferral and Variance Accounts*

9.2.1 In addition to the PP&E clearance, the Applicant is seeking relief with respect to pension and OPEB costs from 2011 onwards. This has two components: a charge of $619,000 to ratepayers for 2011 and 2012, and a variance account going forward to deal with annual fluctuations in the accounting charges for pensions and OPEBs.

9.2.2 With respect to 2011 and 2012, there is no deferral or variance account in place, and the amount in question is less than the materiality threshold of the Applicant. Since the amount cannot be cleared from an existing account, and cannot be treated as a Z factor due to materiality, it would appear to us that there is no route to approve its recoverability without offending the rule against retroactive ratemaking.

9.2.3 Therefore, with respect to 2011 and 2012, it is submitted that recovery should not be ordered.

9.2.4 With respect to 2013 and beyond, the Applicant proposes a variance account. In general, SEC supports the use of variance accounts for these costs, using a relatively long disposition period so that the effect is to capture smoothing of the costs over time, much like the old CGAAP methods did. A variance account of this type has been approved by the Board for Hydro Ottawa in EB-2011-0054, and SEC supported that structure.

9.2.5 Enersource is in a slightly different situation, because it has provided no evidence that the entries in this account would be material. Normally the Board is loathe to establish variance accounts unless the impact is likely to be material.

9.2.6 Notwithstanding this general rule, SEC believes that in this case a variance account should be established, along the lines of that approved for Hydro Ottawa, because the annual adjustments in pension and OPEBs are very unpredictable, and are sensitive to small changes in long-term interest and discount rates. To protect both ratepayers and shareholders, it is submitted that this variance account should be established. In the event that amounts accumulating in the account turn out not to be material, the Board can deal with that at the time disposition is being proposed.

9.3 *Identification of Impacts*

9.3.1 SEC believes that the Applicant has in this Application identified and provided for all of the material impacts of IFRS.

10 SMART METERS

10.1 ***Smart Meter Costs***

10.1.1 No submissions.

10.2 ***Stranded Meters***

10.2.1 No submissions.

11 OTHER MATTERS

11.1 ***Effective Date***

11.1.1 The Applicant is seeking an effective date of January 1, 2013. In light of the timing of the Application, SEC believes it is appropriate that new rates be effective on that date.

11.2 ***Costs***

11.2.1 The School Energy Coalition 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.

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Jay Shepherd
Counsel for the School Energy Coalition