POWERSTREAM INC.

2013 RATES - EB-2012-0161

FINAL ARGUMENT OF THE CONSUMERS COUNCIL OF CANADA

INTRODUCTION:

1. On May 12, 2012 PowerStream Inc. ("PowerStream") filed an Application with the Ontario Energy Board ("Board")for approval of distribution rates effective January 1, 2013. A Settlement Conference was convened on October 3 resulting in a comprehensive Settlement Agreement. On October 29 an oral hearing was held to deal with four outstanding issues.

2. The four remaining issues are:

1. Issue 1.2 - Is the proposed Rate Base for Test Year 2013 appropriate (partially settled);
2. Issue 4.2 - Is the proposed level of depreciation/amortization expense appropriate;
3. Issue 6.1 - Are the proposed test year cost of capital parameters appropriate? (partially settled);
4. Issue 8.2 - Is the treatment of property, plant and equipment due to the transition to the new accounting standard appropriate?

3. The Consumers Council of Canada ("Council") participated in the Settlement Conference and was a signatory to the Settlement Agreement filed with the Board on October 24, 2012. These are the submissions of the Council on the remaining issues.

SUBMISSIONS:

Issue 2.1 Is the proposed Rate Base for Test Year 2013 appropriate?

4. The reason that this issue remains unsettled is that the level of rate base set out in the Settlement Agreement may change depending on how what the Board decides with respect to Issue 2.1. Therefore the Council has no separate submissions to make on this issue.

Issue 4.2 Is the proposed level of depreciation/amortization expense appropriate?

5. As set out in the Settlement Agreement there are two unsettled issues that deal with the proposed level of depreciation.

6. The first issue is whether the 2013 depreciation expense should be determined using the standard "half-year rule", or as requested by PowerStream, should it be determined on a "full-year" basis. Powerstream is seeking approval to apply a full year of depreciation for all 2013 in-service capital additions. If the Board were to accept PowerStream's approach the test year depreciation would increase by $1.883 million. The increase in the 2013 revenue requirement would be $2.527 million. (Ex. JT 1.5)

7. PowerStream has argued that the use of the full year approach is appropriate for the Incentive Regulation Mechanism ("IRM"). The 2013 capital additions would attract a full year of depreciation in 2014 and the subsequent years of the IRM. From PowerStream's perspective using the half year approach "creates a significant funding shortfall during the IRM period." (Argument-in -Chief, p. 6)

8. If PowerStream's rates are set assuming a full year of depreciation, PowerStream's depreciation expense for the test year would be overstated by $1.9 million. In effect PowerStream is seeking approval to collect $1.9 million more from ratepayers than its actual depreciation expense. It is not requesting that, on an ongoing basis depreciation be determined using this approach, but rather that this represents a one-time request (Tr. Vol. 1, p. 41). The Council does not support this approach for the following reasons.

9. The Board approved policy is to determine depreciation for the test year on the basis of the half-year rule. The premise is that assets go into service throughout the year, so on average, assets are assumed in-service for half of the year. If the Board were to change this policy it should only do so through a generic process. PowerStream has not provided any evidence to demonstrate that it should be treated differently than the other local distribution companies ("LDCs") in the Province with respect to depreciation.

10. As noted above granting the relief requested by PowerStream would require ratepayers to pay, in the test year approximately $1.9 more than PowerStream's actual depreciation. It would also result in rate base being $1.9 million higher at the end of 2013 because they have actually taken less depreciation (Tr. Vol. 1, p. 42) From the Council's perspective, this is simply not fair. In addition, Powerstream has admitted that if the Board does not grant this request, it will not defer any of the proposed capital spending in the test year. In effect, the half-year approach is not affecting PowerStream's ability to fund capital in the test year (TC Transcript p. 119).

11. From the Council's perspective PowerStream's proposal is effectively "cherry-picking." If PowerStream is urging the Board to consider the full impact of the 2013 capital additions in 2014 it cannot do so on the basis of depreciation alone. As was discussed at length at the hearing, there are other impacts that arise assuming a full year of capital additions in 2013. These include the impact of assets that have been fully depreciated in 2013 (so no depreciation in 2014), the full-year impact of revenue from new customer additions, and an increase in capital cost allowance ("CCA") (Tr. Vol. 1, p. 45-54)

12. PowerStream has indicated that the depreciation proposal is being advance to deal with capital funding requirements in 2014 throughout the next IRM term. It is not to address issues in the test year which is the subject of this application. It is important to note that given the recent release of the Board's Renewed Regulatory Framework for Electricity ("RRFE"), the current IRM framework will change in 2014. It is not clear what type of rate-making approach will apply to PowerStream in 2014. Accordingly, it would be premature for the Board to approve its PowerStream's request to determine depreciation based on teh full-year approach.

13. The Council notes that PowerStream and other LDCs argued for a change to the current depreciation policy during the RRFE Consultation Process (Tr. Vol. 1, p. 54-55). The Board, in its Report, did not adopt any proposals to change the current, approved approach to depreciation.

14. The second depreciation issue that was not settled was the issue of what is the appropriate methodology for calculating depreciation for 2012 and beyond given PowerStream moved to a monthly in-service date approach in 2010 for financial reporting purposes. PowerStream is of the view that this approach is more accurate than the half-year rule (Tr. Vol. 1, p. 55). PowerStream, however, had its rates set in 2009 on the basis of the half-year rule.

15. If the Board rejects the full-year methodology for 2013, the issue is whether PowerStream should apply the half year rule, or use the monthly in-service date approach which is a more accurate approach for rate-making purposes. From the Council's perspective we see merit in requiring PowerStream to apply the same methodology for rate-making purposes and recording actual depreciation expenses for financial reporting. Accordingly, the Council supports using the monthly in-service date approach for forecasting depreciation in 2013, if PowerStream continues to use this approach for financial reporting purposes.

Issue 6.1 Are the proposed test year cost of capital parameters appropriate?

16. This issue was partially settled. The unsettled issue is what is the appropriate debt rate to apply to three Promissory Notes held by PowerStream's shareholders. Those notes totalling $166.1 million are:

1. Corporation of the City of Vaughan $78.2 million
2. Corporation of the Town of Markham $67.9 million
3. Corporation of the City of Barrie $20 million

17. The Amended and Restarted Promissory Notes were provided to parties on October 12, 2012. The current rate PowerStream is seeking to recover in rates is 5.58%. The question for the Board, in this proceeding is whether, consistent with the Report of the Board on the Cost of Capital for Ontario's Regulated Utilities (EB-2009-0084) dated December 11, 2009, the current deemed rate of 4.41% should apply.

18. From the Council's perspective PowerStream has an obligation to undertake financing arrangements that are the best interests of its ratepayers. In this case, the Council submits that the interests of its shareholders have clearly taken precedent over the interests of its ratepayers.

19. In the Board's Report it states:

> Third-party debt with a fixed rate will normally be afforded the actual or forecasted rate, which is presumed to be a "market rate". However, the Board recognizes a deemed long-term debt rate continues to be required and this rate will be determined and published by the Board. The deemed long-term debt rate will act as a proxy or ceiling for what would be considered to be a market-based rate by the Board in certain circumstances. These circumstances include:
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> - For affiliate debt (i.e. debt held by an affiliated party as defined by the Business Corporations Act, 1990) with a fixed rate, the deemed long-term debt rate at the time of issuance will be used as a ceiling on the rate allowed for that debt.
> - For debt that has a variable rate, the deemed long-term rate will be a ceiling on the rate allowed for that debt. This applies whether the debt holder is an affiliate or a third-party.
> - The deemed long-term debt rate will be used where an electricity distribution utility has not actual debt.
> - For debt that is callable on demand (within the test year period), the deemed long-term debt rate will be a ceiling on the rate allowed for that debt. Debt that is callable, but not within the period to the end of the test year, will have its debt considered as if it is not callable; that is the debt cost will be treated in accordance with other guidelines pertaining to actual , affiliated or variable-rate debt.

- A Board panel will determine the debt instrument, including the rate allowed based on the record before it and considering the Board's policy (these Guidelines) and practice. The onus will be on the utility to establish the need and prudence of its actual and forecasted debt, including the cost of such debt. (Cost of Capital Report, pp. 53-54)

20. The Council submits that the 4.41% rate should apply as the notes have variable rates. The promissory notes all have provisions that the interest rates may/will be adjusted from time to time as agreeable by the Cities in order to reflect current market conditions, the deemed interest rate as prescribed by the Ontario Energy Board and the same interest rate for similar debt owed to all shareholders of any successor. (Tr. Vol. 1, p. 72-76).

21. The Council is taking no position on whether the notes are callable within the test year. Having said that, to the extent the Board determines that they are callable, clearly the Board's deemed rate should apply as this is consistent with the Board's Guidelines.

22. In August 2012 PowerStream issued $200 million of new debt at a rate of 3.99%. This demonstrates that the 5.58% rate requested by PowerStream is far too high. As noted above , the Council is of the view that PowerStream has an obligation to undertake financing arrangements that are in the best interests of its ratepayers. PowerStream has admitted that it could have refinanced the $166.5 million at the time it issued the new debt (Tr. Vol. 1, p. 80). In addition, PowerStream's witnesses admitted that it did not speak to city representatives about whether they should get a lower rate or if PowerStream could pay them out and get lower cost debt (Tr. Vol. 1, p. 83).

23. If PowerStream has decided that it intends to maintain the current financing arrangements with its shareholders it can do so. For rate-making purposes, however, the Council submits that the Board should either apply a rate of 3.99% to the entire $366 million or apply the deemed rate of 4.41%. PowerStream had financing options available to it that were more favourable to the ratepayers. It chose not to make those arrangements, instead deciding to maintain the existing arrangements for the $166.1 million. From the Council's perspective that choice was inappropriate. There is no reason to require ratepayers to fund debt at rates that are well above current market rates, when it there is clear evidence that market rates could be obtained.

Issue 8.2 Is the treatment of property, plant and equipment due to the transition to the new accounting standard appropriate?

24. As a result of moving from CGAAP on IFRS on January 1, 2011 PowerStream has included the difference in overheads capitalized between CGAAP and IFRS on both rate base and construction work in progress ("CWIP") as of the end of 2012 in Account 1575. This deferral account was approved by the Board on June 13, 2011 ("PP&E account") to record the changes in property, plant and equipment related to the changes in accounting standards. The unresolved issue is whether the difference in CWIP should be included in the account.

25. The Council has reviewed the submissions of Board Staff regarding this issue and agrees with the analysis provided. Board Staff has pointed out that the Board did not grant a generic variance account to mitigate volatility in certain expenses that may arise from the application of IFRS standards. In addition, Board Staff notes that PowerStream's interpretation of the Addendum Report (Addendum to the Report of the Board on IFRS, June 13, 2011) is incorrect. Including CWIP and its associated overhead costs in Rate Base PP&E is a departure from the Board policy and should be disallowed. (Board Staff Submission, dated November 12, 2012)

26. Board Staff identified a second sub-issue. That issue is: Notwithstanding the fact that PowerStream may have departed from the Addendum Report, should the Board approve the cost recovery of one of the impacts of PowerStream's transition from CGAAP to IFRS as at January 1, 2011, arising from an accounting change to capitalization of burden and overhead costs which resulted in increases to PowerStream's 2012 OM&A expenses? With respect to recovery the Council supports the submissions of Energy Probe, that is that the recovery should be based on the after-tax impact of the difference in CWIP at the end of 2012 as a result of the change from CGAAP to IFRS.

COSTS:

27. The Council requests that it be awarded 100% of its reasonably incurred costs.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

November 12, 2012