

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

**AND IN THE MATTER OF** an application by E.L.K. Energy Inc. for an order approving just and reasonable rates and other charges for electricity distribution to be effective October 1, 2010.

**E.L.K. ENERGY INC.**

**REPLY TO APRIL 8, 2013 BOARD STAFF SUBMISSION ON SETTLEMENT PROPOSAL**

**FILED APRIL 15, 2013**

**INTRODUCTION:**

1. E.L.K. Energy Inc. (“E.L.K.”) carries on the business of distributing electricity within the Towns of Essex, Lakeshore and Kingsville as described in its distribution licence. Within these towns, which cover a large geographic area in Southwestern Ontario, E.L.K. has six non-contiguous service areas, serving the communities of Belle River, Comber, Cottam, Essex, Harrow and Kingsville.
2. E.L.K. filed an application with the Ontario Energy Board (the “Board”) on October 24, 2012 under section 78 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15 (Schedule B), seeking approval for changes to the rates that E.L.K. charges for electricity distribution, to be effective October 1, 2012 (the Application”). The Board assigned the Application File Number EB-2011-0099.
3. Five parties requested and were granted intervenor status: the Association of Major Power Consumers in Ontario (“AMPCO”); Energy Probe Research Foundation (“Energy Probe” or “EP”), EnWin Utilities (“EnWin”), the School Energy Coalition (“SEC”); and the Vulnerable Energy Consumers’ Coalition (“VECC”). These parties are referred to collectively as the “Intervenors”.
4. Pursuant to Procedural Order No. 3, E.L.K. and the Intervenors, with the exception of EnWin, participated in a Settlement Conference on February 28, 2013. E.L.K. and the Intervenors that participated in the Settlement Conference are collectively referred to below as the “Parties”.
5. The Parties achieved a complete settlement on all issues in the proceeding, and on March 28, 2013, E.L.K. filed the Settlement Agreement on behalf of the Parties. Although EnWin did not participate in the Settlement Conference, by letter dated April 5, 2013, EnWin wrote to the Board to confirm that it had no objection to the Settlement Agreement.

6. By letter and submission dated April 8, 2013, Board Staff have discussed two matters related to the Settlement Agreement.

- First, Staff are concerned about the Parties' approach to the determination and disposition of the balance in Account 1562 (Deferred PILs) under Issue 10.1 (Are the account balances, cost allocation methodology and disposition period appropriate?); and
- Second, Board Staff have not opposed the Parties' proposed treatment of changes to E.L.K.'s depreciation rates and capitalization policies as discussed under Issues 2.4 and 4.2. The Parties have agreed that during 2013, E.L.K., together with its accounting advisors, will determine appropriate depreciation rates taking into consideration the recent Kinectrics Report on useful lives, and in addition will adjust its capitalization policy as required. The Parties have agreed that E.L.K. should use deferral account 1576 – Accounting Changes Under GAAP – to record 2012 adjustments to E.L.K.'s PP&E once this has been completed. The difference in the December 31, 2012 rate base resulting from the application in 2012 of the new depreciation rates and changes in the capitalization policy will be recorded in account 1576, and subject to the Board's approval of the new depreciation rates and changes in the capitalization policy, this amount will be disposed of as part of E.L.K.'s 2014 IRM rate application. Board Staff note that the Board's description of Account 1576 in Appendix A to its July 17, 2012 letter regarding *Regulatory accounting policy direction regarding changes to depreciation expense and capitalization policies in 2012 and 2013*. "among other things, specifies that 'The amount of the cumulative variance recorded in this account would be recovered from, or refunded to, ratepayers **in the year of the distributor's cost of service application** (emphasis added) through an adjustment to depreciation expense over the approved amortization period.'" Board Staff suggest that for future clarity, the Board may wish to acknowledge that the treatment agreed upon by the Parties differs from the Board's description of Account 1576.

7. E.L.K. offers the following submissions in respect of these two matters.

**ACCOUNT 1562 DEFERRED PILS DISPOSITION:**

8. According to the Settlement Agreement, certain matters would be addressed in E.L.K.'s 2014 IRM Rate Application (among the terms of the settlement was that although this was an application for

2012 rates, E.L.K. would not make an IRM rate adjustment application for 2013). These items included the following:

- Under Issue 2.4 (Is the capitalization policy and allocation procedure appropriate?), the parties agreed as follows,<sup>1</sup> with a similar provision included under Issue 4.2 (Is the proposed level of depreciation/amortization expense for the test year appropriate?)<sup>2</sup>:

For the purposes of settlement, the Parties have provisionally accepted E.L.K.'s capitalization policy as it was set out in Exhibit 2, Tab 1, Schedule 1 of the original Application, subject to the following adjustments. The Parties acknowledge that E.L.K. is not converting to International Financial Reporting Standards ("IFRS") in the 2012 Test Year and will remain on CGAAP until required by the Accounting Standards Board (the "AcSB") to move to IFRS. E.L.K. has sought to comply with the Board's letter titled "Regulatory accounting policy direction regarding changes to depreciation expense and capitalization policies 2013" dated July 17, 2012. However, for the purposes of settlement, the Parties accept that E.L.K. will require time to consider the appropriate useful lives for its distribution assets and to determine the regulatory accounting changes for its depreciation expense and capitalization policies. During 2013, E.L.K., together with its accounting advisors, will determine appropriate depreciation rates taking into consideration the recent Kinectrics Report on useful lives, and in addition will adjust its capitalization policy as required. The Parties have agreed that E.L.K. should use deferral account 1576 – Accounting Changes Under GAAP – to record 2012 adjustments to E.L.K.'s PP&E once this has been completed. The difference in the December 31, 2012 rate base resulting from the application in 2012 of the new depreciation rates and changes in the capitalization policy will be recorded in account 1576. Subject to the Board's approval of the new depreciation rates and changes in the capitalization policy, this amount will be disposed of as part of E.L.K.'s 2014 IRM rate application. In addition, the models used to support the rates set out in this proposed Settlement Agreement will be rerun to reflect the new depreciation rates and capitalization policy. The rates resulting from the rerun of the models will be used as the starting rates for the 2014 IRM rate application.

- Under Issue 10.1 (Are the account balances, cost allocation methodology and disposition period appropriate?), the Parties agreed as follows:<sup>3</sup>

"...the Parties have agreed to the disposition of 50% of all Group 1 and Group 2 account balances as set out in Board Staff IR #39 (d) over the 12 month period commencing on the effective date of the Rate Order arising out of this proceeding. The Parties note that Account 1562 is being addressed separately in this Settlement Agreement for the reasons discussed below. The Parties have agreed that the amounts remaining for disposition will be determined through a suitable audit process. In this regard, the Parties respectfully request that the Board direct the Regulatory Accounting and Audit branch of the Board to conduct an audit of E.L.K.'s Group 1 and Group 2 account balances at a time that is mutually acceptable to E.L.K. and the Board. The Parties have agreed that the results of the audit

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<sup>1</sup> Settlement Agreement, at p.16

<sup>2</sup> Settlement Agreement, at p.25

<sup>3</sup> Settlement Agreement, at p.41

would be addressed by E.L.K. in its 2014 IRM rate adjustment application, the intention being that the Board would determine the final outstanding amounts to be authorized for disposition commencing May 1, 2014.”

- Also under Issue 10.1, the Parties agreed as follows with respect to the treatment of Account 1562 (Deferred PILs):<sup>4</sup>

With respect to the disposition of balance in Account 1562 (Deferred Payment in Lieu of Taxes), E.L.K. had originally calculated this balance as \$40,047 recoverable from customers. In discussions with Board Staff, it appears that the balance may actually be an amount of \$751,938 payable to customers. The Parties have agreed for the purpose of settlement to the payment to customers of 50% of the \$751,938 over a 36 month period commencing on the effective date of the rate order arising out of this proceeding. The Parties respectfully request that E.L.K. be allowed the proper time to review and analyze all activity in this account and subsequently to undergo a regulatory audit or other detailed review of this account by the Board if the Board determines such an audit or detailed review is required. The Parties have agreed that the results of this review by E.L.K. or the Board, or a regulatory audit by the Board, would be addressed by E.L.K. in its 2014 IRM rate adjustment application, the intention being that the Board would then determine the final outstanding amounts to be authorized for disposition, commencing May 1, 2014 and the appropriate disposition period would then be addressed.

9. Board Staff have not taken issue with the Parties’ proposed approach to the first two of these three matters – in other words, Board Staff accept that changes to E.L.K.’s depreciation rates and capitalization policy, and the determination of Group 1 and 2 account balances will be coming forward in E.L.K.’s 2014 IRM application. However, instead of accepting that the third of these items will also come forward in the 2014 IRM application, Board Staff have suggested adding another phase to the current, settled proceeding to deal with this one item. Staff suggest that the calculation of the Account 1562 balance is the result of a mechanical process, so that they do not see the need for further analysis and review on E.L.K.’s part; and Staff do not see that E.L.K.’s circumstances warrant an extended timeline for the review of Account 1562 balance in light of the Board’s expectation, expressed in its June 2011 Decision on the Combined Proceeding for Account 1562 PILs (EB-2008-0381), that distributors would file for final disposition of their Account 1562 balances in their next rate applications (either IRM or cost of service).
10. E.L.K. respectfully submits that the Board should not adopt the Staff approach, for the following reasons:

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<sup>4</sup> Settlement Agreement, at p.41

- If the Settlement Agreement is approved by the Board, two of the three items set out above will be coming before the Board in E.L.K.'s 2014 IRM application, due to be filed by the fall of this year. E.L.K. would anticipate that the Intervenors in the current proceeding will have notice of, and an opportunity to participate in the 2014 IRM proceeding in respect of these items. E.L.K. submits that it is more efficient and cost-effective to deal with Account 1562 in the same IRM proceeding rather than having the Board create an additional process in the current settled proceeding to deal with one item, with the attendant additional costs in utility time and resources and Intervenor cost awards. Creating another process in the current proceeding does not avoid intervenor involvement in the 2014 IRM application and it risks diverting E.L.K. resources from work on the 2014 IRM application which will be due later this year.
- While Board Staff suggest that the Account 1562 calculation is mechanical, the facts are that E.L.K. had originally calculated this balance as \$40,047 recoverable from customers, and that Board Staff have calculated a balance of \$751,938 payable to customers. This is a very large change of approximately \$800,000 from the original calculation, and it arose in the later stages of this proceeding. E.L.K. submits that this is a significant amount of money for the utility – by way of comparison, the revenue deficiency following the settlement is only \$461,055. E.L.K. submits that it is reasonable and appropriate that it have an opportunity to review this matter with its consultant and, if necessary, with the Board. With E.L.K.'s 2014 IRM application due later this year, E.L.K. is not seeking a great length of time for this review.
- As for the Board Staff observation with respect to the Board's Decision on the Combined Proceeding for Account 1562 PILs (EB-2008-0381) that distributors would file for final disposition of their Account 1562 balances in their next rate applications, E.L.K. did file for final disposition in the current Application. However, having been advised of a potential \$800,000 adjustment in the calculation, it is appropriate to allow E.L.K. time to investigate the matter.
- E.L.K.'s customers are not being prejudiced by the Parties' approach to Account 1562. The Settlement Agreement provides for the disposition of 50% of the Account 1562 balance based on the Board Staff calculation, so that customers are already receiving funds, subject to the

review of the calculations and the making of any necessary adjustments to the amount for disposition.

- Finally, it is clear that this approach will not result in a large number of similar requests from other distributors. As Board Staff confirm at page 2 of their submission, “Other than for E.L.K., there remains only one other electricity distributor whose account 1562 has yet to be heard by the Board; and this application is to be filed shortly.”

11. For all of the foregoing reasons, E.L.K. respectfully requests that the Board approve the Settlement Agreement as presented, and that it reject the Board Staff request for an additional process in the current settled proceeding in respect of Account 1562.

**DISPOSITION OF ACCOUNT 1576 – ACCOUNTING CHANGES UNDER CGAAP:**

12. Based on its understanding that Board Staff are not suggesting any change in the Parties’ proposed treatment of Account 1576, and that the suggestion is only that the Board note that its approved treatment of Account 1576 in this proceeding differs from its description in the July 17, 2012 letter, then E.L.K. does not object to such a clarification.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 15<sup>TH</sup> DAY OF APRIL, 2013:

E.L.K. ENERGY INC.  
Per:

*Original signed by Mark Danelon*

Mark Danelon  
Manager, Finance and Regulatory Affairs