

Ontario Energy Board

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 Kitchener-
Wilmot Hydro Inc. for an order approving just and reasonable
rates and other charges for electricity distribution to be
effective January 1, 2014.

**ENERGY PROBE RESEARCH FOUNDATION
("ENERGY PROBE")**

ARGUMENT

January 23, 2014

**KITCHENER-WILMOT HYDRO INC.
2014 RATES**

EB-2013-0147

ARGUMENT OF ENERGY PROBE RESEARCH FOUNDATION

A - INTRODUCTION

This is the Final Argument of the Energy Probe Research Foundation ("Energy Probe") related to the issues that were not completely settled in the setting of 2014 rates for Kitchener-Wilmot Hydro Inc. ("KWHI") to be effective January 1, 2014.

In particular, as set out in the Settlement Agreement dated December 3, 2013, there are three issues with a status of "No Settlement". These are issues 1.1 - Has KWHI responded appropriately to all relevant Board directions from previous proceedings?; Issue 2.2 - Is the WCA for the test year appropriate; and Issue 4.1 - Is the overall OM&A forecast for the test year appropriate?

There are also a number of issues in the Settlement Agreement with a status of "Incomplete Settlement". Energy Probe makes no submissions on any of these issues as they all relate only to changes that would need to be incorporated based on the Ontario Energy Board ("Board") determination of Issues 2.2 and 4.1 noted above. Should the Board make changes in either or both of these areas, Energy Probe submits that the Board should make provision for a review of the changes that KWHI will need to make for each of these "Incomplete Settlement" issues through the draft rate order process, including the relevant working papers.

This Argument has been structured to reflect the above noted issues. Where readily available, Energy Probe has attempted to provide the impact of its submissions on the revenue requirement of KWHI. However, in order to minimize intervenor time and costs, a comprehensive impact analysis has not been undertaken. If the Board accepts any or all of the Energy Probe submissions, it is assumed that the direct and indirect impacts would be determined by KWHI and reviewed by intervenors and Board Staff through the associated draft rate order process.

B - SUBMISSIONS

Issue 1.1 - Has KWHI responded appropriately to all relevant Board directions from previous proceedings?

The unsettled issue here relates to the direction from the Board in the EB-2009-0267 application for 2010 rates regarding the working capital allowance and the need for KWHI to prepare a lead-lag study for its' next cost of service application.

In the April 7, 2010 Decision and Order, the Board stated:

KW Hydro has proposed to conduct a lead-lag study in the preparation of its next cost of service rebasing application. The Board finds this proposal timely and appropriate; the Board notes that KW Hydro will have implemented smart meters and Time-of-Use ("TOU") rates by that time. The standard 15% formula is dated and has not been reviewed for a while, and there have been many changes in utility operations, and changes in technology and productivity.

The Board notes that the appropriateness of the level of working capital is also being raised in other applications, and that the Board may initiate a generic proceeding/consultation on determining a new working capital methodology in advance of KW Hydro's next cost of service filing. In such case, the Board expects that KW Hydro will participate in such a process and will take into account the outcomes of such a process. The Board expects that KW Hydro will support its cash working capital allowance in its next rebasing application based on the outcomes of this Board-led process or based on the lead/lag study that KW Hydro stated it would individually undertake. (pages 26-27)

In his opening remarks, Mr. Van Ooteghem indicated that KWHI did not do a lead-lag study because the Board issued a letter on April 12, 2012 that set the default percentage to 13%, which was what KWHI used in the current application in the absence of a lead-lag study (Tr. Vol. 1, pages 31-32).

Specifically, the Board stated in the April 12, 2012 letter, that it would not require distributors to file lead-lag studies for 2013 rates, unless they are required to do so as a result of a previous Board decision. This is the statement that KWHI relies on for not doing a lead-lag study as part of this application. Furthermore, KWHI stated that it believed that the Board's April 12, 2012 letter was equivalent to a Board-initiated generic proceeding or consultation (Tr. Vol. 1, pages 34-36).

Energy Probe respectfully submits that the Board's April 12, 2012 letter was simply an update to the filing requirements for transmission and distribution applications. The letter is clearly labeled as "Update to Chapter 2 of the Filing Requirements for Transmission and Distribution Applications - Allowance for Working Capital". Energy Probe submits that this update to the filing requirements is not equivalent to a Board initiated or Board led process. The Board decision in EB-2009-0267 specifically refers to a generic proceeding/consultation. In the response to 2-Energy Probe-15 KWHI could not provide a Board file number related to this generic proceeding/consultation. This is because no such proceeding or consultation took place.

Further, the Board stated that it expected KWHI to participate in any such generic/consultative process. KWHI confirmed that it did not participate in such a process (Tr. Vol. 1, page 35).

Energy Probe submits that KWHI should have followed the Board's directive and filed a lead-lag study given that there was no generic proceeding/consultative in which the Board expected KWHI to participate.

Energy Probe further submits that KWHI should have consulted with Board Staff and intervenors with respect to the obligation to do the lead-lag study in advance of making the unilateral decision to not do one based solely on its interpretation of the directive.

Issue 2.2 - Is the WCA for the test year appropriate?

There are two outstanding issues with respect to the whether or not the WCA for the test year is appropriate. The first is the level of OM&A included in the calculation of the WCA. The level of the OM&A is dealt with under Issue 4.1 below.

The second issue is the appropriate percentage to be applied to the sum of the cost of power and OM&A expenses. KWHI has used a factor of 13%, based on the Board's April 12, 2012 letter discussed under the previous section.

Energy Probe submits that this percentage is significantly too high for KWHI.

a) The Move to Monthly Billing

Regardless of whether or not KWHI should have filed a lead-lag study as a result of the EB-2009-0267 Decision, Energy Probe submits that KWHI should have submitted a lead-lag study for the test year because of the decision to move to monthly billing.

KWHI currently bills its residential, GS < 50 kW and MicroFIT customers on a bi-monthly basis. The remainder of the customers are billed on a monthly basis. KWHI proposes to move all customers to monthly billing for the 2014 test year (2-Energy Probe-16). The reason for doing this is to assist customers with cash flow concerns due to rising electricity bills (Exhibit 2, Tab 2, Schedule 2, page 4).

Energy Probe generally supports the move to monthly billing, but only if it is done properly. Energy Probe submits that KWHI has not done a proper analysis as part of this application.

KWHI has only done an analysis of the increase in costs related to office supplies and postage (4-Staff-20d). The cost increase associated with this change is \$401,500, as included in the 2012 test year forecast (Undertaking JT1.15). However, as acknowledged in Undertaking J1.2, these costs will actually be higher because of the recent announcement by Canada Post of increased postage rates. This would add another \$98,000 to the costs, bringing the total cost to close to \$500,000 (Tr. Vol. 1, page 36).

As part of the response to Undertaking J1.2, KWHI indicates that there may be an additional cost of \$94,000 per year if an additional collector is needed. As a result the total potential costs are close to \$600,000 per year.

However, KWHI has not done a business case for the change to monthly billing (Tr. Vol. 1, page 50). KWHI, while agreeing that the move to monthly billing would more closely match the inflows of revenue with the monthly billing of electricity costs from the IESO (4-Energy Probe-71) states that it cannot quantify the impact of the improved cash flow because it did not do a lead-lag study.

Energy Probe submits that this change is precisely why a lead-lag study should have been undertaken. The improvement in cash flow is one of the biggest benefits to the distributor of monthly billing as compared to bi-monthly billing. This ties the flow of revenues much more closely to the monthly payment of the cost of power to the IESO, as acknowledged by KWHI. As shown in the Review Requirement Workform attached as Appendix D to the Settlement Agreement, the cost of power expense makes up more than 91% of the costs to which the WCA is applied.

The Util-Assist report on moving to monthly billing (Exhibit K1.2, pages 17 to 23), while not a business case, is described by the authors of the report as '*a "listing" of the benefits which other Ontario LDCs have reported in recent years*' (Section 1.2). However, as shown in the response to Undertaking J1.2, KWHI disagrees with most of the benefits reported by other LDCs in Ontario, such as reduced collections, bad debt write-offs, number of payment arrangements made, reduction in customer calls and so on. It would appear that KWHI, for some unknown reason, is different from other distributors in Ontario.

However, as confirmed by the KWHI witnesses, KWHI did not talk to any other distributors that had moved from bi-monthly to monthly billing (Tr. Vol. 1, page 52). Thus, KWHI has failed to explain why it is different from other distributors and it has failed to learn from others with respect to the move to monthly billing.

Energy Probe submits that the onus is on the utility to present a case for the change it is proposing. KWHI has not met this onus due to the lack of a business case that would establish both costs and benefits of moving to monthly billing; KWHI believes that the move to monthly billing will result in cost increases where other distributors have found cost decreases; KWHI failed to complete a lead-lag study to quantify the beneficial impacts of improved cash flow. In short, KWHI only quantified cost increases to customers, not cost decreases.

b) Remedies for the Lack of Lead-Lag Study

Energy Probe submits that the Board should not accept the move to monthly billing as proposed by KWHI without some modifications.

In particular, Energy Probe submits that there are two options that the Board should consider related to this matter.

i) Deny Approval for the Move to Monthly Billing

The Board could simply deny approval for the \$401,500 included in the 2014 test year OM&A forecast associated with the costs of moving to monthly billing. Further, the Board could direct KWHI to complete a full business case, including a lead-lag study, to be filed before or as part of its next rebasing application, if it proposes to move to monthly billing in that rebasing application.

ii) Adjust WCA to Reflect the Impact on the Service Lag

Energy Probe notes that KWHI does not believe that the WCA should be updated to reflect the proposal to move a number of its rate classes to monthly billing. Energy Probe respectfully submits that the Board should adjust the WCA if it approves the costs associated with monthly billing. To do otherwise would burden customers with additional costs while ignoring the obvious benefits to KWHI in terms of cash flow. These benefits need to be passed on as cost reductions to ratepayers. Anything else could not and would not result in just and reasonable rates.

A Board Decision changing the WCA to reflect the move to monthly billing would be consistent with the decision in EB-2009-0096 (Decision with Reasons dated April 9, 2010, pages 27-29) for Hydro One Networks Inc. wherein the Board concluded that it would make an adjustment to the working capital allowance to recognize the impact of the shift from bi-monthly to monthly billing. As indicated in that Decision, Hydro One was moving about 140,000 customers to monthly billing, representing about 11% of their customers, whereas the impact on KWHI is much more significant, with 96% of the customers being switched to monthly billing (Tr. Vol. 1, pages 44-45).

In the submission that follows below in part (c), Energy Probe provides a simple methodology to reduce the 13% WCA used by KWHI to reflect the movement to monthly billing. Energy Probe submits that the Board should approve a WCA of 9.365% for the 2014 test year. Details of how this figure are provided in part (c) below.

iii) Preferred Option

Energy Probe submits that the preferred option is to adjust the WCA to reflect the impact on the service lag component of the WCA percentage. As noted earlier, Energy Probe supports the movement to monthly billing, assuming benefits, and not just costs, for customers are properly accounted for.

While denying the costs associated with moving to monthly billing is the simplest solution, it is not in the best of interest of customers. They would have to wait until 2019 to receive monthly invoices. Energy Probe submits that this is not reasonable.

c) Calculation of an Appropriate WCA for KWHI

i) Use of the Default 13% Information

Energy Probe submits that it is reasonable to assume that the Board's update to the filing requirements in the April 12, 2012 letter was based on the electricity distribution lead-lag studies that the Board had seen and approved at that time. The following table summarizes the electricity distribution lead-lag studies that the Board had seen and approved when the filing requirement change from 15% to 13% was made.

Table 1

<u>FILE NO.</u>	<u>DISTRIBUTOR</u>	<u>WC %</u>
EB-2011-0054	HYDRO OTTAWA	14.20%
EB-2010-0131	HORIZON UTILITIES	13.50%
EB-2007-0680 (1)	TORONTO HYDRO	12.90%
EB-2009-0096 (2)	HYDRO ONE DIST.	<u>11.50%</u>
AVERAGE		13.03%

The calculation of the WCA percentage is the result of the difference in days between a revenue lag and an expense lead, divided by the number of days in the year.

Mathematically, the lead-lag formula is a simple difference of two figures:

$$(\text{REVENUE LAG}/365) - (\text{EXPENSE LEAD}/365) = (\text{NET LAG DAYS}/365)$$

The revenue lag is further divided into specific components, being the service lag, billing lag, collection lag and payment processing lag. These are standard revenue related lags and are defined in lead-lag studies. For example, the lead-lag study for Navigant Utilities from Exhibit 2, Tab 4, Schedule 1, Appendix 2-3 in EB-2010-0131 (and included at pages 29 through 49 of Exhibit K1.2 in this proceeding), and are not repeated here.

The following table summarizes the components of the revenue lag from the lead-lag studies of the four distributors that were available to the Board before it changed the WCA to 13%.

Table 2

		SERVICE	BILLING	COLLECTION	PAYMENT PROCESSING	TOTAL REVENUE
<u>FILE NO.</u>	<u>DISTRIBUTOR</u>	<u>LAG</u>	<u>LAG</u>	<u>LAG</u>	<u>LAG</u>	<u>LAG</u>
EB-2011-0054	HYDRO OTTAWA	30.24	18.11	25.47	1.15	74.97
EB-2010-0131	HORIZON UTILITIES	30.27	17.35	24.00	1.21	72.83
EB-2007-0680	TORONTO HYDRO	27.10	16.17	27.06	1.43	71.76
EB-2009-0096	HYDRO ONE DIST.	<u>21.00</u>	<u>19.12</u>	<u>32.07</u>	<u>0.00</u>	<u>72.19</u>
AVERAGE		27.15	17.69	27.15	0.95	72.94

The information used to populate Table 2 is found in the various lead-lag studies filed in the individual applications. The figures are taken from the relevant parts of these studies, which were included in pages 29 through 59 of Exhibit K1.2.

The move to monthly billing primarily impacts the service lag. This lag measures the time from the distributor's provision of electricity to a customer to the time the customer's service period ends and the meter is read.

Based on the mid-point methodology used in lead-lag studies, a monthly service period has a service lag of 15.21 days, while a bi-monthly service period has a lag of 30.42 days. These two lags are simply the calculation of the number of days in the year (365) and the number of service periods in the year (12 for monthly, 6 for bi-monthly), divided by 2.

The service lag is then simply a weighted average of the 15.21 and 30.42 figures, with the weights being the number of customers that are billed monthly and bi-monthly, respectively.

As can be seen by the service lags in the above table, none of the distributors in the group which was used by the Board to set the WCA at 13% bills all of its customers on a monthly basis.

As KWHI agreed, when they go to monthly billing, their service lag will decline to 15.21 days (Tr. Vol. 1, page 70).

The Board's current WCA default value of 13% does not take into consideration the mix of monthly and bi-monthly invoiced customers. The 13% default is equivalent to a net lag days of 47.45 days (13% of 365 days in the year). Combined with the average revenue lag of 72.94 days as calculated in Table 2, the average expense lead days is simply the difference between these figures, or 25.49 days (Tr. Vol. 1, page 68).

With respect to the billing, collection and payment processing lag, Energy Probe submits that KWHI is not likely to be significantly different from the average of the four distributors shown in Table 2. KWHI agreed with this (Tr. Vol. 1, pages 63-64). Similarly, KWHI agreed that overall, there was no reason to expect that the expense leads for KWHI would be any different from that of the four distributors (Tr. Vol. 1, pages 64-65). This is especially true when considering that the cost of power expense represents about 91% of the controllable costs and cost of power to which the WCA is applied and the fact that payment deadlines associated with the cost of power are standard across the electricity industry in Ontario (Tr. Vol. 1, pages 65-65).

KWHI further agreed that there would be no impact of moving to monthly billing on the expense leads, the billing lag or the payment processing lag (Tr. Vol. 1, pages 65-66). KWHI indicated that they were not sure about the impact on the collection lag, but only insofar as the impact of a change in the threshold that KWHI would set as the amount that they would actively pursue for collections (Tr. Vol. 1, page 67). KWHI further indicated it had not fully examined any change in this threshold from that currently used.

Energy Probe submits that the evidence is clear that moving to monthly billing does not impact the revenue lag days or expense lead days with the obvious exception of shortening the service lag to 15.21 days. In the absence of changing the company's policy with respect to the threshold for active collections, the collection lag is likely to decrease as well, but Energy Probe is not making any recommendation that reflects such a change.

KWHI may not necessarily agree that each of the components of the revenue lag (excluding the service lag) and the expense leads are directly applicable to it. However, in the absence of a lead-lag study and given that KWHI believes the 13% should apply to it, and given that the 13% is based on these exact same averages, Energy Probe submits that using these figures for KWHI is appropriate.

The average 72.94 revenue lag shown in Table 2 includes an average service lag of 27.15 days. Replacing this service lag with the agreed upon 15.21 day lag for KWHI reduces the total revenue lag to 61.00 days. With an average expense lead of 25.49 days, the net lag days is calculated as 35.51 (61.00 - 25.49). This represents a WCA of 9.73%.

ii) Specific Adjustment for KWHI Service Lag

A simpler alternative to the approach discussed at length above is to just reflect the change in the service lag that is specific to KWHI as an adjustment to the 13% WCA.

KWHI has forecast that it will have 90,407 customers that are current billed on a bi-monthly basis that will move to monthly billing in 2014. The remaining 3,428 forecast customers are already on monthly billing. Based on these weights, KWHI agreed that their current weighted service lag is 29.86 days (Tr. Vol. 1, pages 69-70).

When all customers are moved to monthly billing, the service lag falls to 15.21 days, a decline of 14.65 days. Given that there are no other changes in any of the other components of the revenue lag or in the expense leads associated with the move to monthly billing (discussed in the previous section), this results in a reduction of 14.65 days in the net lag days. This 14.65 day reduction, when divided by 365 days in the year, results in a reduction of 4.0% in the WCA from 13% to 9%.

iii) Recommendation

Energy Probe submits that the Board should reduce the WCA for KWHI associated with the move to monthly billing from 13% as applied for to 9.365%, being the average of two results calculated above. Energy Probe submit that this is an appropriate WCA percentage for KWHI, in the absence of a company specific lead-lag study. It relies on both the averages for the lags and leads from the four distributors shown in Table 1 which the Board relied on to set the default value of 13% along with the change in the service lag from the average for those distributors used in the first method and on the KWHI specific change in the service lag used in the second method. Both methods highlight the fact that the service lag is the only lag or lead component of the analysis that is impacted by the move to monthly billing.

As a check on whether or not the 9.365% is a reasonable level for a WCA for a distributor that bills monthly, Energy Probe notes that in the response to Board Staff at Exhibit K2, Issue 2.2, Interrogatory #2 in EB-2011-0054, Hydro Ottawa indicated that when they move to monthly billing, their WCA would fall to 9.6%.

iv) London Hydro WCA

Energy Probe notes that the Board has one additional lead-lag study that has been filed and approved since it issued its letter in April, 2012. That study was for London Hydro in EB-2012-0146. This study was the first the Board had seen and approved for an electricity distributor that billed all of its customers on a monthly basis. KWHI stated that they did not believe the London Hydro study would be comparable to the situation that KWHI found itself in because London Hydro bills for water.

Energy Probe agrees with KWHI that London Hydro's results should not be factored into the analysis done above because of the water billing performed by London Hydro. While this water billing would not impact the service lag, payment processing lag or any of the expense leads, Energy Probe submits that the billing lag may be higher because of the additional time to create the bills. Similarly, the collection lag may also be higher because of the higher bills being collected. In short, the revenue lag for London Hydro is probably higher than what it would be if it only billed for electricity due to the inclusion of water billing.

d) Ratepayer Impact of the WCA Change

A reduction of 100 basis points in the WCA has the impact reducing costs to ratepayers by \$161,429 per year. The calculation of this figure, shown on page 71, Section 2 of Exhibit K1.2 is based on controllable expenses & cost of power from the Settlement

Agreement and the pre-tax return of 7.74% on rate base. Ms. Nanninga accepted these calculations (Tr. Vol. 1, page 72).

The proposed reduction in the allowed WCA from 13.0% to 9.365% to reflect the move to monthly billing for all customer classes for KWHI results in a reduction in costs to ratepayers of \$586,794. This figure is calculated by multiplying the difference in the WCA of 3.635% times the figure of \$161,429 noted in the previous paragraph.

The actual impact of the reduction in the WCA from 13% to the proposed 9.365% would, of course, also be impacted by any reduction in the OM&A forecast which is dealt with below in Issue 4.1.

Issue 4.1 - Is the overall OM&A forecast for the test year appropriate?

a) The Requested Increase

KWHI is requesting approval of an OM&A forecast of \$18,480,760 for the 2014 test year. This is an increase of 6% from the bridge year forecast of \$17,431,075, which in turn is an increase of 11.3% over the last year of actual expenditures for 2012. These figures are summarized in the table below.

Table 3

	New CGAAP 2012	New CGAAP 2013	New CGAAP 2014
Final as Filed (1)	16,390,832	17,431,075	18,480,760
Adj. for Smart Meter Decision (2)	-731,974	0	0
Final as Filed after Smart Meter Adj.	15,658,858	17,431,075	18,480,760
% Change		11.3%	6.0%
(1) Undertaking JT1.15			
(2) 2-Energy Probe-30			

As can be seen in the above table, each of the years shown is under New CGAAP accounting. Figures for 2012 have been adjusted to remove the smart meter related expenditures incurred prior to 2012 but recorded in OM&A in 2012 as a result of the smart meter decision.

Energy Probe submits that these increases for the 2013 bridge year and the 2014 test year are not appropriate, and not supported by the evidence in the proceeding.

b) Line by Line Forecast Comparisons

In the EB-2009-0267 Decision and Order dated April 7, 2010 for KWHI for electricity rates effective May, 2010, the Board stated (page 13):

"The Board finds it useful to look at OM&A levels from a number of perspectives: the specifics of the test year forecast; trends in spending over time, expectations for inflation and economic conditions; and comparisons with other distributors."

Energy Probe concurs with those comments. However, in this proceeding, it has become apparent that it is not possible to compare the specific spending forecast for the test year to the years before 2012, including the Board Approved figures for 2010.

This comparison is not possible because of the change in accounting from Old to New CGAAP effective January 1, 2012, along with the impact of the smart meter decision. While both of these changes can be accounted for at the total OM&A level, they cannot be accounted for at either the account level or the program level. As a result, a comparison of specific line items is not possible, but a comparison at the total OM&A level is possible.

c) Envelope Approach to OM&A

As noted above, a comparison of total OM&A costs is possible despite the accounting changes and impacts of the smart meter decision on the quantification of OM&A expenditures.

However, as reflected in his opening remarks, Mr. Van Ooteghem stated that KWHI had not experienced a typical year since before the 2010 cost of service application due to a number of reasons (Tr. Vol. 1, pages 24-25). 2009 and 2010 were atypical because of the diversion of resources from OM&A to capital related to the construction of a transformer station. 2011 costs included additional OM&A costs related to deferred maintenance from previous years, again related to the construction of the transformer station. Energy Probe accepts that these years were atypical and does not believe that any valid or relevant comparisons can be made between them or the test year forecast.

However, it is submitted that relevant comparisons can be made on an envelope basis based on three comparisons, each of which is discussed below.

i) 2010 Board Approved OM&A Levels

Energy Probe submits that the first way to look at the overall OM&A increase forecast for the 2014 bridge year is to look at the last Board approved figure for the 2010 test year in EB-2009-2067. This figure would then be adjusted for inflation, customer growth and expected productivity changes in 2011 through 2014.

Table 4 below shows the actual inflation for 2011 through 2012 and the Board figures used for 2013 and 2014 IRM applications, along with the base productivity and stretch factors for the relevant years that are specific to KWHI. The customer growth figures are derived from the evidence, as noted in the footnote.

Table 4

					2010-2014
<u>Escalators</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>Compounded</u>
Inflation (1)	2.30%	1.90%	1.60%	1.70%	1.87%
Base Productivity	-0.72%	-0.72%	-0.72%	0.00%	-0.54%
Stretch Factor	-0.20%	-0.20%	-0.20%	-0.15%	-0.19%
Customer Growth (2)	<u>1.54%</u>	<u>1.51%</u>	<u>1.51%</u>	<u>1.54%</u>	<u>1.52%</u>
Total Escalator	2.92%	2.49%	2.19%	3.09%	2.67%
(1) 2011-2012 actual, 2013-2014 Board Forecast					
(2) Exhibit 4, Tab 1, Schedule 2, Table 4-6					

The compound annual growth rate of the total escalator between 2010 to 2014 is 2.67%. This increase reflects compound annual increases for inflation of 1.87% and 1.52% for customer growth, offset by productivity and stretch factor improvements over the period of 0.54% and 0.19%, respectively.

Energy Probe submits that by applying this compound growth rate to the Board Approved 2010 level of expenditures should provide a reasonable estimate of 2014 expenditures.

The 2010 Board Approved figure was \$13,881,502 (4-Energy Probe-33). On top of this, Energy Probe submits that it is appropriate to add the actual smart meter expenses of \$162,424 (4-Energy Probe-30), to arrive at a base level of expenditures of \$14,043,926. Increasing this figure by 2.67% per year for 2011 through 2014 results in a 2014 figure of \$15,604,964. However, since this figure is based on Old CGAAP, it needs to be increased by \$1,692,337, which is the impact on OM&A of converting to New CGAAP (4-Energy Probe-68 & Tech. Conf. Tr. Vol. 1, page 46). This results in a New CGAAP OM&A forecast of \$17,297,301. This is a reduction of \$1,183,459, or 6.4% from the 2014 forecast of \$18,480,760 shown in Table 3.

ii) Most Recent Information Available

In the response to Undertaking J1.9, KWHI noted that its Board of Directors approved an interim OM&A budget for 2014 on December 6, 2013. This budget is said to be interim until a decision on the current rates application is issued and that a final budget for 2014 will be presented to the Board of Directors following the outcome of this process.

As shown in the Total OM&A line in the table attached to the undertaking response, the budget has been reduced to \$17,999,700. Of this amount, \$20,000 is related to non-LEAP donations which are not recoverable through rates, leaving a budget of \$17,979,700.

While this represents a more reasonable 3.1% over the bridge year forecast, Energy Probe submits that the 2013 bridge year forecast is significantly overstated.

An increase of 3.1% in 2014 over 2013 is reasonable as is illustrated in Table 4 above. Inflation and customer growth offset by a stretch factor of 0.15% and no base productivity results in an increase of 3.1%.

However, as noted above, the 2013 bridge year forecast is significantly over forecast. As noted in the response to Undertaking J1.3, the year-to-date November, 2013 actual OM&A expenditures are only 1.6% higher than the expenditures for the same period in 2012 and total \$15,322,700. Applying a 1.6% increase to the actual 2012 OM&A expenses adjusted for the removal of prior year smart meter expenditures results in a 2013 estimate of \$15,567,863.

Energy Probe submits that the increase of 1.6% in 2013 costs over 2012 may be understated based on the figures in Table 4. In particular, Energy Probe submits that an increase of 2.2% for 2013 is an appropriate reflection of changes in inflation, customers and productivity and stretch factors.

Starting with the adjusted 2012 actual OM&A expenses and increasing them by 2.2% for 2013 and 3.1% for 2013 results in a 2014 forecast of \$16,499,457. This is a reduction from the test year forecast included in the revenue requirement of \$1,981,303, or 10.7%.

iii) Average OM&A Cost Per Customer Analysis

Based on the response to Undertaking J1.7, KWHI had 89,025 customers in 2012. This is contrast to the figure of 91,020 customers found in Exhibit 4, Tab 1, Schedule 2, Table 4-6. That figure is actually customers/connections.

Based on the smart meter adjusted actual OM&A expenses of \$15,658,858 shown in Table 3 and the above noted 89,205 customers, the actual 2012 OM&A per customer cost was \$175.89.

Energy Probe has used the 2012 figure as the appropriate starting point for the same reasons noted earlier about the atypical costs incurred in 2009 through 2011. The 2012 figure does not need to be adjusted for accounting changes, and the smart meter change is a straight forward adjustment to the 2012 figure.

Increasing this value for 2013 inflation, and assuming no base productivity or stretch factor improvements, whatsoever, in both 2013 and 2014 results in inflationary increases of 1.6% in 2013 and 1.7% in 2014 (see Table 4). Applying these increases to the 2012 figure of \$175.54 per customer results in a 2014 cost per customer of \$181.75.

Energy Probe was unable to find the forecasted number of customers (rather than customers/connections) in the evidence. As a result, Energy Probe has calculated the 2014 number of customers to be 91,761. This figure reflects the starting point of 2012 actual customers of 89,025 as reported in Undertaking J1.7, increased by the growth rate in customer/connections found in Exhibit 3 of 1.51% in 2013 and 1.54% in 2014, both of which are shown in Table 4 above.

Applying the forecasted cost per customer of \$181.75 to the forecasted number of customers results in an OM&A forecast of \$16,677,108. No adjustment is need for accounting changes since the accounting change took place in 2012. This results in a reduction to the OM&A forecast of \$1,803,652, or 9.7%.

d) OM&A Forecast Accuracy

Energy Probe notes that KWHI has a history of over forecasting OM&A expenses as part of its rate applications for both bridge and test years.

In the EB-2009-0267 proceeding, KWHI forecasted bridge year expenditures for 2009 of \$13,331,700 and \$14,190,476 for the 2010 test year (EB-2009-0267 Decision and Order, page 9). The Board approved 2010 OM&A expenditures of \$13,881,502 and with the adjustment for smart meters added to this figure, totalled \$14,043,927.

Actual OM&A costs, including allocated smart meter costs, were \$12,366,033 or \$966,000 or 7.2% below forecast for the 2009 bridge year (4-Energy Probe-30 & 4-Energy Probe-33). Actual 2010 costs were \$12,433,381 or \$1,757,000 or 12.4% below the forecast and \$1,610,000 or 11.5% below the Board approved figure.

Similarly, KWHI has forecast OM&A expenses for the 2013 bridge year to be \$17,431,075, an increase of 11.3% over the smart meter adjusted levels for 2012 (see Table 3).

However, as noted in the response to Undertaking J1.3, the year-to-date November, 2013 actual OM&A expenditures are only 1.6% higher than the expenditures for the same period in 2012 and total \$15,322,700.

KWHI qualifies these numbers by indicating that year-to-date costs as of November, 2013 is not indicative of 11/12 of year end costs given the ice storm of December, 2013 and further year-end adjustments and accruals that are made during the year.

Energy Probe submits that any costs incurred in 2013 as a result of the ice storm would not be reflected in a typical year of expenditures. Furthermore, these costs may well be brought forward by KWHI for Z factor recovery.

As for year-end adjustments, Energy Probe acknowledges that year-to-date figures cannot be prorated on a straight line basis to determine the full year figures. However, KWHI has not provided any evidence to suggest that the year-end adjustments and accruals that will be made for 2013 were any different than those made for 2012 or other years.

As a result, Energy Probe submits that based on 11 months of actuals, it would be reasonable to estimate 2013 OM&A expenditures to be 1.6% higher than in 2012. This would result in 2013 OM&A expenditures of approximately \$15,909,400 (\$15,658,858 from Table 3, increased by 1.6%). This represents a reduction of \$1,522,000 or 8.7% from the current bridge year forecast.

Over the three years in question (2009, 2010 and 2013), the average level of over forecast OM&A expenses is more than \$1.4 million and 9.4%.

e) Recommendation

Energy Probe submits that an appropriate reduction to OM&A expenses for the 2014 test year is \$1,656,138 from the forecast of \$18,480,760 to \$16,824,622. This reduction is the average of the reductions calculated in sections (i), (ii) and (iii) in part (c) above. This is a reduction of approximately 9% from the updated forecast.

Energy Probe submits that this reduction is reasonable given the robust analysis used to generate the 3 figures above, and is similar to the over forecasts noted in part (d) above of previous KWHI OM&A forecasts used for cost of service applications.

The proposed reduction of \$1,656,138 is inclusive of the \$401,500 related to the incremental costs associated with the move to monthly billing. If the Board were to disallow these costs as part of Issue 2.2 discussed above, then the additional reduction proposed by Energy Probe would be approximately \$1.25 million.

C - COSTS

Energy Probe requests that it be awarded 100% of its reasonably incurred costs. Energy Probe co-operated with other intervenors in this application to minimize duplication where possible. Energy Probe took a lead position in the working capital analysis issue while other intervenors took a lead position on the OM&A issue.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

January 23, 2014

**Randy Aiken
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