

**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 Hydro One  
Brampton Networks Inc. for an order approving just and  
reasonable rates and other charges for electricity distribution to  
be effective January 1, 2015.

---

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

**ARGUMENT**

---

**November 3, 2014**

**HYDRO ONE BRAMPTON NETWORKS INC.  
2015 RATES APPLICATION**

**EB-2014-0083**

**ARGUMENT OF ENERGY PROBE RESEARCH FOUNDATION**

**A- INTRODUCTION**

Hydro One Brampton Networks Inc. ("HOBNI") filed a Settlement Agreement in this proceeding with the Board on October 9, 2014. The Board approved the Settlement Agreement as filed (Tr. Vol. 1, page 2).

This is the Argument of the Energy Probe Research Foundation ("Energy Probe") related to the unsettled issues in this proceeding. These unsettled issues are as follows:

- a) The determination of the correct amount for disposition in Account 1576 - Accounting Changes under CGAAP Deferral Account and the appropriate disposition period;
- b) The methodology used to forecast degree days used in the regression equation; and
- c) The appropriate percentage to be used to calculate the Working Capital Allowance.

**B - SUBMISSIONS**

**a) The determination of the correct amount for disposition in Account 1576 - Accounting Changes under CGAAP Deferral Account and the appropriate disposition period**

Energy Probe submits that there are two distinct issues related to Account 1576. These issues are the correct amount for disposition in the account and the appropriate disposition period for the amount to be recovered from ratepayers.

**i) Correct Amount**

With respect to the first issue, HOBNI is requesting the recovery, over 5 years, of \$6,622,303. This figure, which is comprised of \$4,835,562 as the difference in the closing net PP&E (former CGAAP vs. revised CGAAP) and a return on rate base associated with this balance at the weighted average cost of capital of 7.39%. These figures are all taken from Appendix 1 to Exhibit 9, Tab 4, Schedule 1, which is Appendix 2-EE.

HOBNI agreed that this amount would change as a result of changes in the weighted average cost of capital that will result from the Board's updates for 2015 cost of service applications (Tr. Vol. 1, page 14). Energy Probe agrees with this change, as it is consistent with the Settlement Agreement (page 28-29) that the cost of capital parameters will be updated to reflect these updates which are expected in November, 2014.

Energy Probe submits that there is a change to the difference in the closing net PP&E (\$4,835,562) that the Board should direct HOBNI to make. The change relates to the use of the half-year rule for the depreciation in the 2014 bridge year.

The difference in the net PP&E as shown in Appendix 2-EE is based on the difference in the closing net PP&E values for 2013 and 2014 between the former CGAAP and the revised CGAAP. The HOBNI witnesses have confirmed that under the former CGAAP, the depreciation expense for both 2013 and 2014 was calculated using the half year-rule. Energy Probe submits that this is appropriate because the half-year rule was utilized under the former CGAAP accounting methodology.

With respect to the closing net PP&E balance under the revised CGAAP methodology, the number in Appendix 2-EE is \$332,295,594. This figure is identical to and consistent with the figure shown in the fixed asset continuity schedule for 2014 in Exhibit 2, Tab 2, Schedule 2, page 5, as it should be.

As explained by HOBNI during cross-examination, the actual 2013 depreciation expense and the resulting net PP&E were based on the in-service depreciation methodology, as was required under IFRS (Tr. Vol. 1, pages 20-21). However, there was confusion as to what was used in 2014 for the purposes of the continuity schedule and Account 1576. Mr. Gapic indicated that the depreciation expense (and hence the closing net PP&E) for 2014 reflected the half-year methodology, but then indicated that he thought it could be implied that it was based on the month in-service methodology (Tr. Vol. 1, page 21). When asked if the number included in Account 1576 for net depreciation (\$12,038,606 as shown in Appendix 2-EE) was not consistent with the continuity schedule for PP&E, Mr. Gapic indicated that HOBNI used the half-year rule for the 2014 bridge year (Tr. Vol. 1, page 22).

The response to 4-Energy Probe-36a clearly states that:

*"The half year rule is utilized for the forecasts of the bridge and test years and for the historical years (except for 2013 actual). HOBNI started the monthly in-service methodology in 2013 for its actual depreciation expense calculation and will continue as required under the IFRS accounting standard."*

Energy Probe submits that the net depreciation expense shown in Appendix 2-EE for 2014 for Account 1576 is identical to that shown in the 2014 continuity schedule in Exhibit 2, Tab 2, Schedule 2, Appendix 1. The \$12,038,606 in Account 1576 is equal to additions to accumulated depreciation (\$14,276,258) less disposals of accumulated depreciation (\$2,237,652).

Since the depreciation figures and, indeed, the closing net PP&E figures for 2014 are identical in Account 1576 and in the 2014 PP&E continuity schedule and because the continuity schedules are based on the half-year methodology, it is clear that the figure shown in Account 1576 for 2014 under the revised CGAAP methodology is incorrect in that it reflects the half-year methodology, rather than the in-service methodology that is required for IFRS and has been used for the revised CGAAP figures for 2013 in Account 1576 (Tr. Vol. 1, page 21).

Energy Probe submits that the amount in Account 1576 at the end of 2014 under the revised CGAAP methodology should be adjusted to reflect the in-service methodology that is required under IFRS. Energy Probe further submits that the increase in the net PP&E at the end of 2014 (as a result of lower depreciation expense in 2014 using in-service as compared to half-year depreciation) under revised CGAAP should be \$142,000. This is approximately the midway point between the reduction in depreciation expense in 2013 of \$140,779 (4-Energy Probe-36b) and the agreed to reduction in the 2015 test year of \$144,000 (Settlement Agreement, page 21).

This reduction in the depreciation expense would result in higher net PP&E under revised CGAAP, thereby reducing the amount to be recovered from ratepayers by an equivalent amount, plus weighted average cost of capital over the recovery period.

#### ii) Disposition Period

Energy Probe submits that the Board should direct HOBNI to recover the amounts in Account 1576 over 3 years rather than over 5 years, as proposed by HOBNI. The reason for this is the impact on ratepayers.

As shown in the response to Undertaking J1.1, the total amount to be recovered from rate payers under a 3 year disposition period is \$5,907,606. This is a reduction of approximately \$715,000 from the amount that would be paid by ratepayers over the 5 years proposed by HOBNI.

Based on a simple net present value calculation using a discount rate of HOBNI's weighted average cost of capital, or 7.39%, the cost to ratepayers is less if the costs are recovered over a 3 year period (\$5,131,205) than it is over a 5 year period (\$5,374,310), as shown in the following table.

**Table 1**

<b><u>NET PRESENT VALUE CALCULATIONS FOR ACCOUNT 1576</u></b>							
	<b><u>Year 1</u></b>	<b><u>Year 2</u></b>	<b><u>Year 3</u></b>	<b><u>Year 4</u></b>	<b><u>Year 5</u></b>	<b><u>Total</u></b>	<b><u>NPV</u></b>
3 Year Disposition	\$1,969,202	\$1,969,202	\$1,969,202	\$0	\$0	\$5,907,606	\$5,131,205
5 Year Disposition	<u>\$1,324,461</u>	<u>\$1,324,461</u>	<u>\$1,324,461</u>	<u>\$1,324,461</u>	<u>\$1,324,461</u>	<u>\$6,622,303</u>	<u>\$5,374,310</u>
Difference	\$644,741	\$644,741	\$644,741	-\$1,324,461	-\$1,324,461	-\$714,697	-\$243,105
Discount Rate	7.39%						

Energy Probe notes that the Filing Guidelines for Electricity Distribution Rate Applications - 2014 Edition for 2015 Rates Applications dated July 18, 2014 ("Filing Requirement") state that the *"Board's determination of the disposition period will be on a case-by case basis and will be guided primarily by such considerations as bill impacts and the financial impact on distributors"* (page 64).

Energy Probe submits that the Board's description of how it would determine on a case-by-case basis was premised on the situation in which distributors were required to refund amounts in Account 1576 to ratepayers. Under these circumstances the Board would take into account the ability of the distributor to pay the amounts to ratepayers in one year or whether a longer term was required. It would also be based on the bill impacts to customers where, for example, a reduction in one year would be followed by a significant increase in the following year if the amount in the account were rebated to customers over 1 year.

However, as noted by HOBNI (Tr. Vol. 1, pages 12-13), it has a balance in Account 1576 that is recoverable from ratepayers, but unlike the other distributors that had a 5 year disposition approved by the Board, HOBNI is collecting this money from ratepayers rather than refunding it.

Energy Probe submits that HOBNI has no issues with the financial impact on it, since if it did, it would have sought recovery over a shorter period. HOBNI selected 5 years due to the availability of the weighted average cost of capital being returned to the company as well, even though HOBNI did not need to recover the amount from ratepayers over a shorter period of time (Tr. Vol. 1, page 17).

With respect to the impact on bills, Energy Probe notes that the 5 year recovery period resulted in an increase of \$0.24 per month, compared to a total bill of \$117.31 at current Board approved rates for a typical residential customers consuming 800 kWh of power per month (Settlement Agreement, Appendix 2-W). This amounts to 0.2% of the current bill. The move to a 3 year recovery period increases the charge to \$0.40 per month on the same bill, resulting in an increase of 0.34% (Undertaking J1.1). The impact on other rate classes is similar to that for the residential class.

Energy Probe submits that there is no need to extend the recovery period to 5 years based on bill impacts to customers. Further, as noted earlier, there is no adverse financial impact on HOBNI of accelerating the recovery of the amounts in the account, unlike the distributors that were granted a 5 year disposition period to rebate their amounts to their ratepayers (Tr. Vol. 1, pages 12-13).

Energy Probe further notes that the Report of the Board - Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach dated October 18, 2012 ("RRFE") states that the renewed regulatory framework is a comprehensive performance-based approach to regulation that is based on the achievement of outcomes and the provision of value for money for customers. The emphasis is be on results rather than activities and will better respond to customer preferences.

The outcome of the HOBNI proposal for a 5 year disposition period as compared to the 3 years proposed by Energy Probe is that ratepayers are worse off, paying more than \$700,000 more on a cash flow basis under the 5 year proposal. This is a negative outcome for ratepayers.

On a value for money basis, the net present value calculations show that the cost of the HOBNI 5 year proposal is more than the 3 year proposal. This reflects that ratepayers would receive less value for their money under the HOBNI proposal.

Energy Probe notes that the Board is also placing greater emphasis on customer feedback and preferences under the RRFE.

HOBNI provided the results of its customer engagement in Exhibit 1, Tab 6, Schedule 1. In particular, Figure #1 provides a list of the one or two most important things to customers from the survey undertaken.

The most important thing to customers was better prices/lower rates, at 50%. This was far and away the most important thing to customers, with the next highest item, better communication with customers, coming in at 11%.

Energy Probe submits that customers have made their preferences quite clear to HOBNI and to the Board. Rates, and by default costs, are extremely important to customers. Recovery over the shorter 3 year period provides more value to customers than a longer recovery period because it costs them less both on a net present value basis and over the longer term and reflects customer preferences with respect to the rates and prices being the most important issues to these customers.

In summary, Energy Probe submits that the Board should direct HOBNI to dispose of the balance in Account 1576 over a 3 year period.

**b) The methodology used to forecast degree days used in the regression equation**

This issue deals solely with the methodology used to forecast the degree days used in calculating the load forecast.

HOBNI proposes to use a 10 year average to forecast normal degree days. Energy Probe submits that HOBNI has not provided any analysis that supports the use of the 10 year average. The onus is on the distributor to provide evidence in support of their proposal. HOBNI provided no such credible evidence.

In their last cost of service proceeding, HOBNI forecast degree days based on the use of a 30 year average (EB-2010-0132, Exhibit 3, Tab 2, Schedule 2.0, page 3, Filed: 30-June-2010). It is, therefore, clear that HOBNI has changed its methodology used to forecast degree days.

The evidence that HOBNI has filed to support the change to a 10 year average is sparse and does not stand up to scrutiny. In Exhibit 3, Tab 1, Schedule 1, HOBNI states that the current trend in weather pattern that is shown in Table 4 supports the use of the 10 year average. However, all that Table 4 provides is a comparison of two points: the 10 year average for 2004 to 2013 period and the 10 year average for the 1994 to 2003 period. Based on the change in the average for these two periods, HOBNI concludes that there is a trend that shows a decrease in heating degree days and an increase in cooling degree days.

Energy Probe submits that two points do not a trend make. Even if they did, HOBNI did not look at any other methodologies that would provide a forecast for degree days.

In Exhibit K1.1, at pages 10 and 11, HOBNI attempts to illustrate that the 10 year average is a better predictor of degree days than is the 20 year trend.

Energy Probe submits that a review of 9 months is not anywhere close to an adequate period over which to compare the accuracy of the different forecasting methodologies.

Energy Probe also notes that HOBNI failed to follow the Filing Guidelines with respect to providing forecasts based on 20 year trend methodology. The Filing Guidelines are quite specific. In Section 2.6.1.1 (page 228 of Exhibit K1.4), it states that if the monthly heating and cooling degree days are used to determine normal weather, the monthly HDD and CDD based on a) 10-year average and b) a trend based on 20-years is to be included in the explanation of the weather normalization methodology. The Filing Guidelines also state that in addition to the proposed test year load forecast, the load forecasts based on the 10-year average and 20-year trends in HDD and CDD are to be provided, along with the rationale as to why the proposed normal weather methodology was chosen.

During direct examination, Mr. Gagic stated that HOBNI had provided the calculations required in the Filing Guidelines associated with the 20 year average (Tr. Vol. 1, page 28). As noted above, the guidelines require the 20 year trend, not the 20 year average.

HOBNI was asked to provide the 20 year trend forecasts in 3-Energy Probe-15, and responded that the information requested was included in HOBNI's load forecast model submitted to the OEB as part of its original application. However, as noted earlier, that evidence was based on the 20 year average, not the required 20 year trend.

In the response to 3-Energy Probe-56TC, HOBNI provided the 20 year trend forecasts for heating and cooling degree days and the impact on the revenues at existing rates. This was the information that should have been provided if the Filing Requirements had been followed.

Energy Probe notes that HOBNI's own evidence supports the use a trend to forecast degree days. In Exhibit 3, Tab 1, Schedule 1, at pages 7 and 8, HOBNI states that analysis done by it reveals that over time, the average temperature during the summer and winter is increasing. Unfortunately, HOBNI did not follow this up with any analysis based on the 20 year trend as required in the Filing Requirements.

The Board approved the results of a comprehensive evaluation framework for selecting the degree day forecasting methodology in EB-2006-0034. In that Decision, dated July 5, 2007, the Board stated:

*"The Board believes that given that the sole purpose of a forecasting methodology is to accurately forecast weather it is simply appropriate to select a method based on the empirical findings." (page 9)*



In the most recent Decision for Enbridge Gas Distribution Inc. ("Enbridge") (EB-2012-0459 dated July 17, 2014), the Board approved a degree day forecasting methodology for the Central Region (the Greater Toronto Area) based on a 50:50 weighting of a 10 year moving average and a 20 year trend (pages 27-28). Again, this was based on the acceptance of the comprehensive analysis that was performed by Enbridge in arriving at the forecasting methodology that resulted in the more reliable forecast.

This comprehensive analysis compared 10 different forecasting methodologies and ranked them based on accuracy, symmetry and stability of the forecasts over the 1990 through 2012 period. Clearly this analysis is much more comprehensive than the analysis provided by HOBNI.

Energy Probe submits that the Enbridge Decision is relevant in the current proceeding because Enbridge's Central Region includes Brampton and the degree days used by both parties are from the same source, the Toronto International Airport weather station. Furthermore, it provides results that are directly relevant to HOBNI.

The outcome of the Enbridge Decision should be reflected as the appropriate outcome for HOBNI ratepayers, just as it has been reflected for those same ratepayers of Enbridge.

Energy Probe notes that this change would impact not only revenues at existing rates, but would also impact all rate rider calculations both in the current proceeding and in future proceedings that clear deferral and variance accounts. The increase in the volumetric forecast would reduce the rate riders associated with disposition amounts.

In summary, Energy Probe submits HOBNI has failed to provide sufficient rationale for the use of the 10 year average for forecasting degree days. HOBNI has not provided any evidence of why it has moved away from the previous 30 year average. It has not shown that the 10 year average is more accurate, which according to the Board, is the sole purpose of a forecasting methodology for degree days.

Energy Probe submits that the Board should direct HOBNI to use the same 50:50 weighting of the 10 year average and 20 year trend methodologies it approved for use by Enbridge. This outcome is appropriate because it results in the same treatment for customers in Brampton that are both gas and electricity customers. It reflects a comprehensive analysis that has been approved by the Board in selecting the most accurate forecasting methodology. Energy Probe further submits that this is in line with the spirit of the RRFE, that emphasizes results rather than activities and is based on appropriate outcomes.

**c) The appropriate percentage to be used to calculate the Working Capital Allowance**

Energy Probe submits that a working capital allowance ("WCA") percentage of 13%, based on the Filing Guidelines is significantly overstated, is no longer a valid figure that the Board can rely on and violates the spirit of the RRFE.

**i) The 13% Default Value - Where Did It Come From?**

On April 12, 2012 the Board issued a letter related to an *Update to Chapter 2 of the Filing Requirements for Transmission and Distribution Applications - Allowance for Working Capital*.

In that letter, the Board stated (Exhibit K1.4, pages 3-4):

*"...the Board has reviewed the results of lead/lag studies filed by distributors in cost of service applications and in each of those cases both the applied-for WCA and the final Board-approved WCA have been lower than 15%. The Board has determined that it is not appropriate for a default value for WCA to be set at a higher level than those resulting from lead/lag studies. Based on the results of WCA studies filed with the Board in the past few years, the Board has determined that the default value going forward will be 13% of the sum of cost of power and controllable expenses."*

Energy Probe notes that the update to the guidelines for the working capital allowance was not done in a transparent manner as there was no consultation with interested parties as had originally been proposed by the Board. This has resulted in questions as to how the Board determined that a figure of 13% was appropriate.

Energy Probe submits that it is clear that the Board reviewed the results of lead/lag studies filed by distributors in cost of service applications. This is what the above noted letter says. The letter does not say that the Board reviewed the results of some of the lead/lag studies filed by distributors. Nor would this make any sense. The Board would use the results of all the lead/lag studies it would have seen and approved when the letter was issued. It would have had no basis to include some studies/decision while not including other studies/decisions.

This is supported by the Board's Decisions in a number of cases (EB-2011-0130 and EB-2013-0122 are examples) where it states that it did not consider it appropriate to adopt the results of a lead-lag study from another utility without a thorough analysis concluding that the two utilities are comparable. Clearly the Board's guideline is based on its belief that it was appropriate to adopt the results of lead-lag studies and Board decisions from a number of utilities even though those utilities may not be comparable to others.

The question then becomes, how many lead-lag studies and decisions did the Board see before issuing its April 12, 2012 letter. Energy Probe submits that the Board had the results from four lead-lag studies and resulting decisions. These four lead-lag studies and decisions are shown in Table 2 below. A review of applications and decisions prior to April 12, 2012 indicates that these were the only lead-lag studies that were filed by electricity distributors.

As shown in Table 2 the average of the Approved WCA percentages is 13.03%, virtually identical to the default value in the Board's April 12, 2012 letter. Furthermore, as noted in the EB-2014-0198 Draft Report of the Board Electricity and Natural Gas Distributors' Residential Customer Billing Practices and Performance dated September 18, 2014 ("Billing Practices Report"), the Board acknowledges that "*...the Board's current policy on working capital allowance is based on an average approach that has not attempted to quantify the effect on cash flow...*" (page 9) (emphasis added).

Energy Probe therefore submits it is reasonable to conclude that the Board's 13% default value is based on the four electricity distributor lead-lag studies and Board decisions that had been rendered before the issuance of the guideline. There were only four studies and it is reasonable to conclude that the Board included all of them in setting this guideline.

#### ii) Problems With The 13%

There are two glaring problems with the use of the 13% as a default for all electricity distributors. The first deals with the issue of monthly versus bi-monthly billing and the second deals with the calculation of the service lag for those distributors that bill at least some of their customers on a bi-monthly basis.

With respect to the first issue, it is clear that all four of the distributors that filed lead-lag studies and where a decision was made by the Board on the appropriate WCA percentage billed at least some of their customers on a bi-monthly basis. This can be seen in Table 2 by looking at the Service Lag column. If a distributor billed of its customers on a monthly basis, by definition the service lag would be 15.21 days, which is the midpoint of the service period and is calculated as  $((365/12)/2)$ . Similarly, for customers billed on a bi-monthly basis, the service lag is 30.42 days  $((365/6)/2)$ . For customers that bill some customers on a monthly basis and some on a bi-monthly basis, the resulting service lag is somewhere between 15.21 and 30.42 days. As shown in Table 2, all of the service lags are greater than 15.21 days, meaning each of the four distributors billed some of its customers on a bi-monthly basis.

Energy Probe submits that the Board's current policy on the working capital allowance ignores that benefit of monthly billing in terms of improved cash flow. The Board has confirmed this in the Billing Practices Report (page 9) where it states that *"An additional benefit of a change to monthly billing is the improvement in cash flow of the distributors."*

HOBNI currently bills all of its customers on a monthly basis, and has done so for at least 10 years. Energy Probe submits that using a default value for the WCA percentage that is based on distributors that bill on both a monthly and bi-monthly basis for a distributors that bills all customers monthly is not appropriate. As noted earlier, in the EB-2013-0130 Decision and Order dated August 14, 2014, the Board concluded that it was not *"appropriate to adopt the results of a lead-lag study from another utility without a thorough analysis concluding that the two utilities are comparable."* (page 15). Energy Probe submits it is equally inappropriate to adopt the results from the average of a number of lead-lag studies where the utilities included in the average are demonstrably different to HOBNI. A utility that bills all customers monthly is not comparable to utilities that bill customers on both a monthly and bi-monthly basis.

The second issue noted above is calculation of the service lag for each of the distributors used in the calculation of the 13% default value. As is clearly noted in each of the lead-lag studies shown in Table 2 below, the service lag is calculated using customer weights between those that are billed monthly and those that are billed bi-monthly. This can be seen in Exhibit K1.4 for each of the four lead-lag studies shown in Table 2. In particular, page 13 of Exhibit K1.4 (EB-2007-0680 - Toronto Hydro), page 38 of Exhibit K1.4 (EB-2009-0096 - Hydro One Distribution), pages 69 and 81 of Exhibit K1.4 (EB-2010-0131 - Horizon Utilities) and page 92 and 93 of Exhibit K1.4 (EB-2011-0054 - Hydro Ottawa). The last reference clearly demonstrates the calculation of the service lag based on customer weights.

The problem with a service lag calculated using the number of customers to weight the customers that are billed monthly and bi-monthly, is that it does not reflect cash flow, which is what a lead-lag study is supposed to measure.

Each of the four lead-lag studies in the calculation of the average of 13% was performed by Navigant, or reviewed by Navigant. Navigant has, however, revised its methodology in calculating the service lag for utilities that bill both monthly and bi-monthly. This is highlighted in that 3 of the 4 original studies have since been updated - all by Navigant - and the methodology used to calculate the service lag has been changed from customer

weighting to revenue weighting. The rationale for this change is clear and is included in the studies, including the most recent study for Horizon Utilities in EB-2014-0002, where the following is included under Key Concepts (page 161 of Exhibit K1.4):

*"Dollar-Weighting: Both "Leads" and "Lags" should be dollar-weighted where appropriate and where data is available to more accurately reflect the flow of dollars. As an example, suppose that a transaction has a Cash Outflow Lead time of 100 days and its dollar value was \$100. Suppose further that another transaction has a Cash Outflow Lead time of 30 days with a dollar value of \$1M. A simple un-weighted average of the two transactions would give us a Cash Outflow Lead time of 65 days  $([100+30]/2)$ . On the other hand, dollar-weighting the two transactions gives us a Cash Outflow Lead time closer to 30 days; an answer which is more representative of how the dollars actually flowed in this example."*

Equally important is that Navigant describes the old methodology, upon which the Board has set the 13% used in the guides as "obsolete methodology" in reference to the use of customer weighting method for revenue lags (Exhibit K1.4, page 151). This is the most recent Navigant lead-lag study prepared to Hydro One Distribution (EB-2013-0416, Exhibit D1, Tab 1, Schedule 3, Attachment 1).

Energy Probe submits that the Board should not continue to impose a figure of 13% that is based on a clearly out-of-date methodology on ratepayers. Nor should it impose a percentage that is clearly based on an average of utilities that are clearly not comparable when it comes to billing frequency.

### iii) The Correct Approach

Energy Probe submits that the correct approach to determining the appropriate WCA percentage, based on the information before the Board in this proceeding is to simply recalculate the average percentage WCA based on a service lag of 15.21 days that represents the fact that HOBNI bills all of its customers on a monthly basis.

Energy Probe submits that, other than a reduction in the HST, replacing the service lag for each of the four lead-lag studies with 15.21 days, no other component of the revenue lags or expense leads would be changed. The HOBNI witnesses agreed with this (Tr. Vol. 1, page 64).

Energy Probe notes that the change in the HST due to monthly billing is a further reduction in the WCA requirement. This is confirmed and can be seen in the response to 2-Energy Probe-11 in EB-2014-0002 (Exhibit K1.4, pages 179-192). In particular, a comparison of the tables provided in Attachment 1 of that response shows that the only

changes in the working capital requirement of monthly billing as compared to a mixture of monthly and bi-monthly billing is a reduction in the number of days of the service lag (included in the revenue lag) and a reduction in the HST. None of the other lags or leads are impacted.

Energy Probe further notes that by replacing the customer weighted service lag (based on the obsolete methodology) with 15.21 days to reflect monthly billing, eliminates the need to calculate a weighted service lag. This results in key improvements to the Board's out-of-date guideline. First it makes the lead-lag studies used by the Board comparable to HOBNI in that all the figures represent monthly billing. Second, it eliminates the obsolete weighting methodology that has invalidated the 13% because no weighting methodology is needed to calculate the service lag. All of the customers and all of the revenue is based on monthly billing.

Table 2 shows the adjustments proposed by Energy Probe to arrive at a comparable (monthly billing) WCA percentage that does not suffer from an out-of-date obsolete methodology.

**Table 2**

<u>FILE NO.</u>	<u>DISTRIBUTOR</u>	<u>BOARD</u> <u>APPROVED</u>	<u>SERVICE</u> <u>LAG</u>	<u>CHANGE IN</u> <u>SERVICE LAG</u> <u>(e) = 15.21-</u>	<u>% CHANGE IN</u> <u>SERVICE LAG</u>	<u>WCA IF</u> <u>BILLED</u> <u>MONTHLY</u>	
<u>(a)</u>	<u>(b)</u>	<u>(c)</u>	<u>(d)</u>	<u>(d)</u>	<u>(f) = (e)/365</u>	<u>(g) = (c) + (f)</u>	
EB-2007-0680 (1)	TORONTO HYDRO	12.90%	27.10	-11.89	-3.26%	9.64%	(3)
EB-2009-0096 (2)	HYDRO ONE DIST.	11.50%	21.00	-5.79	-1.59%	9.91%	(3)
EB-2010-0131	HORIZON UTIL.	13.50%	30.27	NA	NA	9.00%	(4)
EB-2011-0054	HYDRO OTTAWA	<u>14.20%</u>	<u>30.24</u>	NA	NA	<u>9.60%</u>	(5)
<u>AVERAGE</u>		13.03%	27.15			9.54%	
(1) 12.90% RESULTED FROM EB-2010-0142 - NO CHANGE IN LEAD/LAG STUDY, ONLY CHANGE IN MIX OF COSTS							
(2) SEE EB-2009-0096 DECISION & WORKING PAPERS							
(3) CALCULATED BASED ON A REDUCTION OF SERVICE LAG TO 15.21 DAYS & NO CHANGES TO ANY OTHER COMPONENTS							
(4) EB-2010-0131 INTERROGATORY RESPONSE - EXHIBIT K1.4, PAGES 80-84							
(5) EB-2011-0054 INTERROGATORY RESPONSE - EXHIBIT K1.4, PAGE 115)							

Table 2 adjusts the WCA percentage to reflect monthly billing for Toronto Hydro and Hydro One Distribution. No adjustments are needed for Horizon Utilities or Hydro Ottawa since the response to interrogatories in those proceedings provided the WCA percentages associated with monthly billing.

Other than the reduction in the average WCA percentage, Energy Probe submits that by standardizing the results to reflect monthly billing has reduced the variance or volatility in the WCA percentages. Based on the obsolete method of calculating the service lag, the WCA percentages ranged from 11.50% to 14.2%, for a range of 2.70%. Based on the

adjusted calculations this range is much narrower, ranging from 9.00% to 9.91%, a range of 0.91% or approximately one-third of the original range.

As the above table illustrates, these changes reduce the WCA percentage from 13% to approximately 9.5%.

As noted during cross-examination the impact of a one percentage point reduction in the WCA percentage results in a reduction of about \$435,000 in costs to ratepayers.

Reducing the WCA from 13% to 9.5% would, therefore, result in a reduction of more than \$1.5 million in rates. This reduction represents a significant portion of the base revenue requirement, which is \$69,029,255, as shown in the RRWF attached to the Settlement Agreement. Put another way, the reduction in the working capital allowance of \$1.5 million represents more than 2% of the base revenue requirement.

#### iv) The Correct Approach Extended

Energy Probe notes that HOBNI has provided a table of more recent lead-lag studies in Exhibit K1.1 at page 3. The list includes the updated studies for 3 of the 4 original lead-lag studies. Hydro Ottawa is the only one that has not yet filed an updated study.

Energy Probe submits that the Board may well want to use the most recent studies available to determine an appropriate figure for HOBNI. Energy Probe further notes that the list provided by HOBNI contains 7 lead-lag studies, which is a larger and more robust sample than that used by the Board in determining the 13%.

Using the same approach as in Table 2 and extending it to the larger group of studies included in Exhibit K1.1, Energy Probe has converted the figures provided by HOBNI to the comparable monthly billing calculation of the WCA. In doing this, it should be noted that only 1 of the 7 lead-lag studies shown in the HOBNI exhibit bills on a monthly basis. As can be seen in the Service Lag column of Table 3, this is London Hydro (EB-2012-0146). The results of this approach for the larger and more current sample of lead-lag studies are shown in Table 3 below.

Several of these studies still suffer from the use of the customer weighting lag for the service lag, while the more recent ones (Horizon, Toronto Hydro and Hydro One Distribution) use the revenue weighting. No weighting was required in the London Hydro study.

In addition, as discussed with HOBNI, Energy Probe has corrected the service lags for EB-2014-0002 (Horizon) and EB-2013-0174 (Veridian) to reflect corrections and updates to the evidence in those proceedings for the service lags (Tr. Vol. 1, pages 62-63).



**Table 3**

<u>FILE NO.</u>	<u>DISTRIBUTOR</u>	<u>APPLIED OR</u> <u>APPROVED</u>	<u>SERVICE</u> <u>LAG</u>	<u>CHANGE IN</u> <u>SERVICE LAG</u> <u>(e) = 15.21-</u> <u>(d)</u>	<u>% CHANGE IN</u> <u>SERVICE LAG</u>	<u>WCA IF</u> <u>BILLED</u> <u>MONTHLY</u>	
<u>(a)</u>	<u>(b)</u>	<u>(c)</u>	<u>(d)</u>	<u>(d)</u>	<u>(f) = (e)/365</u>	<u>(g) = (c) + (f)</u>	
EB-2014-0002	HORIZON UTIL.	12.00%	25.02	NA	NA	8.72%	(1)
EB-2013-0416	HYDRO ONE DIST	7.40%	16.40	-1.19	-0.33%	7.07%	
EB-2014-0116	TORONTO HYDRO	7.99%	18.72	-3.51	-0.96%	7.03%	
EB-2013-0174	VERIDIAN	13.40%	22.30	-7.09	-1.94%	11.46%	
EB-2011-0054	HYDRO OTTAWA	14.20%	30.24	NA	NA	9.60%	(2)
EB-2012-0033	ENERSOURCE	13.50%	28.75	-13.54	-3.71%	9.79%	
EB-2012-0146	LONDON HYDRO	<u>11.42%</u>	<u>15.21</u>	0.00	0.00%	<u>11.42%</u>	
		11.42%	22.38			9.30%	
(1) EB-2014-0002 INTERROGATORY RESPONSE - EXHIBIT K1.4, PAGE 179							
(2) EB-2011-0054 INTERROGATORY RESPONSE - EXHIBIT K1.4, PAGE 115							

Table 3 adjusts the WCA percentage to reflect monthly billing for all of the utilities shown except for Horizon Utilities and Hydro Ottawa. No adjustments are needed for either of these utilities since the response to interrogatories in those proceedings provided the WCA percentages associated with monthly billing. As can be seen in Table 3, the adjustment for London Hydro was 0% because their lead-lag study already reflected monthly billing.

As noted with reference to Table 2 earlier, Energy Probe submits that by standardizing the results to reflect monthly billing has reduced the variance or volatility in the WCA percentages. The WCA percentages range from 7.4% to 14.2%, for a range of 6.80%, reflecting a mix of monthly and bi-monthly billing. Based on the adjusted calculations this range is much narrower, ranging from 7.03% to 11.46%, a range of 4.43% or approximately 65% of the original range.

As the above table illustrates, these changes reduce the WCA percentage from 13% to approximately 9.3%. This figure is virtually identical to the 9.5% calculated in Table 2.

Table 3 also clearly shows that the 13.0% average based on the original four lead-lag studies and decisions is now 11.42%, based on the updated studies and larger sample. If Hydro Ottawa is removed this average (because the study is based on the obsolete methodology), the average for the remaining 6 utilities is less than 11%.



#### v) Benchmarking

Energy Probe submits that the use of a default percentage for the WCA is akin to benchmarking. In particular, the utility is being set at a percentage equal to the average percentage of the lead-lag studies and decisions that the Board had seen or issued prior to the release of the April 12, 2012 letter.

Energy Probe has no issues with this concept. However, the benchmark must be reasonable and reliable. In the RRFE (page 56), the Board indicated that benchmarking would become increasingly important, as comparisons among distributors was one means of analyzing whether a given distributor is as efficient as possible. The Board also indicated that the role of benchmarking under the 4th Generation IR rate-setting method was to assess the reasonableness of distributor cost forecasts (page 13).

Energy Probe notes that the working capital allowance is provided in order to allow a distributor to recover its costs associated with financing it requires in order to finance its cash flow requirements.

Thus, any working capital allowance requirement has to be reasonable and in line with its forecasted costs.

In the current proceeding, the benchmark of 13% has been shown to be obsolete and not directly comparable to a utility that bills all of its customers on a monthly basis. When these shortcomings are adjusted for, as has been done in Tables 2 and 3 above, a more appropriate benchmark of 9.5% is arrived at. This benchmark reflects the best information available to the Board at this time.

Given the importance of benchmarking within the RRFE, Energy Probe submits that a correct benchmark needs to be used, and in this case, based on the information the Board has in front of it from several lead-lag studies over the last several years, this benchmark is 9.5%.

#### vi) 13% Default Conflicts with RRFE

Energy Probe submits that the 13% default in the filing guidelines is not compatible with the RRFE.

The RRFE emphasizes outcomes, value for money, customer preferences and customer engagement, none of which are reflected in the 13% default in the filing guidelines. This is not surprising given that the RRFE was issued after the default value was included in the filing guidelines.

Without a doubt, the most important outcome for ratepayers is rates. In survey after survey rates consistently rank at the top of the most important things to ratepayers. HOBNI provided a summary of the results of a customer survey in Figure #1 in Exhibit 1, Tab 6, Schedule 1, which is reproduced here for ease of reference:

One or two most important things 'your local utility' could do to improve service	
Hydro One Brampton	% of all suggestions
Better prices/lower rates	50%
Better communication with customers	11%
Information & incentives on energy conservation	10%
Concerns about SMART meters	9%
Improve power reliability	7%
Improve/simplify/clarify billing	5%
Remove hidden costs on bills	4%
Staff related concerns	4%
Increase service hours/availability of hydro representative	4%
Better on-line presence	4%
Be more efficient	3%
Don't charge for previous debt	2%

Base: total respondents with suggestions

As noted earlier, a one percentage point change in the WCA percentage represents a cost to ratepayers of about \$435,000. Based on the 13% proposed by HOBNI, this amounts to about \$5.66 million, or more than 8% of the base revenue requirement shown in the RRWF attached to the Settlement Agreement. Clearly the revenue requirement associated with the working capital represents a significant component of the rates.

Also included in those rates is the cost associated with monthly billing. With more than 150,000 customers, HOBNI issues more than 1.8 million bills a year. On a bi-monthly basis, this would be about 900,000 a year. The costs associated with monthly billing which include incremental postage, envelopes, paper, payment processing, and other costs are in the neighbourhood of \$1 million a year.

The outcome that is being proposed by HOBNI is that ratepayers are paying for all of the costs associated with monthly billing, but not receiving all of the benefits associated with monthly billing. In particular, ratepayers are not receiving the cost reductions associated with the improvement in cash flow for HOBNI. The Board recognizes that this is an additional benefit associated with monthly billing in the Billing Practices Report noted earlier in this submission. As explained earlier, the default WCA percentage is based on distributors that did not bill on a monthly basis, resulting in a percentage that is higher than for a distributor such as HOBNI that bills monthly.

Energy Probe submits that the improved cash flow is just not an additional benefit, it is the largest benefit to ratepayers. In EB-2013-0159, at Exhibit 4, Appendix A, Oakville Hydro filed a report by util-assist titled Billing Frequency: Moving to Monthly Billing. In section 2.1.1 of that report, it was reported that *"LDCs which have created business cases to justify increasing the billing frequency have found the largest **quantifiable** benefit to be improved cash flow."* (page 4)

By excluding the cash flow benefits from monthly billing in the revenue requirement, Energy Probe submits that the outcome is rates that are higher than they should be. This is a negative outcome under the RRFE that should be corrected.

With regards to customer preferences, Energy Probe notes that customers prefer monthly billing, but not at any cost. The Board has had the opportunity to see many surveys conducted by or for electricity distributors in Ontario. A consistent theme across the survey results is that customers prefer to receive monthly bills, but not if there is an additional cost of \$1 or more per bill.

In the Billing Practices Report, the Board, quite correctly, states that *"it is essential to look at the costs and benefits from both an electricity distributor and customer perspective"* (page 8) in relation to monthly billing.

From the customer perspective, Energy Probe submits that by including the incremental costs associated with monthly billing, while not fully recognizing and reflecting the cost reductions associated with improved cash flow does not and cannot result in value for money for ratepayers. The cost reductions to HOBNI are not being passed on to ratepayers.

There has been no customer engagement and no focus on what customers think is appropriate with respect to the costs associated with billing frequency. Energy Probe submits that educated customers would prefer monthly billing but only if all the benefits and cost reductions are reflected in the rates they pay for this service.

In conclusion, Energy Probe submits that the use of the 13% default guideline for the WCA percentage is not compatible with a regulatory framework that is a comprehensive performance-based approach to regulation that is based on the achievement of outcomes that ensure that Ontario's electricity system provides value for money for customers.

In this particular proceeding, it is clear that the 13% guideline value is obsolete and not reflective of the practice of monthly billing. This results in an unacceptable outcome in terms of rates and clearly does not provide value for money for customers.

#### vii) Summary and Recommendations

Energy Probe submits that the Board cannot rely on the default 13% for setting rates for HOBNI. It has been clearly demonstrated that this figure is based on an obsolete methodology that is out-of-date and did not accurately reflect cash flow requirements.

It is further submitted that the Board should reflect a WCA percentage that is comparable to other utilities if those utilities also billed on a monthly basis, as does HOBNI. This reflects proper benchmarking, a hallmark of the RRFE.

Based on the calculations in Tables 2 and 3 which provide an apples to apples (or in this instance, monthly billing to monthly billing) comparison, Energy Probe submits that the Board should direct HOBNI to use a WCA percentage of 9.5%.

Use of a 9.5% WCA will reduce rates by \$1.5 million a year. Over the term of the IRM plan, this will result in savings to ratepayers of more than \$7.5 million.

Based on the outcome approach of the RRFE and the focus on customers and providing value for money, Energy Probe submits that the Board should not approve the requested 13% as it has been demonstrated that this figure is obsolete and does not reflect a comparable figure for a distributor that bills all customers on a monthly basis.

Given the magnitude of the potential reduction in the base revenue requirement of more than 2% noted above, Energy Probe submits that if the Board approves a 13% WCA for the 2015 test year, it should direct HOBNI to complete a lead-lag study and file it as part of its 2016 IRM application. As part of that application, the study would be examined and the results would be incorporated into the 2016 rate setting process.

It would be inherently unfair for ratepayers of HOBNI to continue to pay \$1.5 million a year, or 2% of their distribution bill, because HOBNI chose to not file a lead-lag study and relied on a default that has been shown to be obsolete and not based on the billing frequency that HOBNI uses and that ratepayers pay for.

## **C - COSTS**

Energy Probe requests that it be awarded 100% of its reasonably incurred costs. Energy Probe worked with other intervenors in this proceeding to ensure complete coverage of the issues with a minimum of duplication.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

**November 3, 2014**

**Randy Aiken  
Consultant to Energy Probe**