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Ontario

BY EMAIL

November 14, 2014

Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: Veridian Connections Inc. ("Veridian")
2015 Z-factor Distribution Rate Application
Board Staff Submission
Board File No. EB-2014-0272

In accordance with Procedural Order #1 please find attached Board Staff's submission in the above noted proceeding. Veridian and the intervenors have been copied on this filing.

Veridian's reply to the submission is due on November 28, 2014.

Yours truly,

Original Signed By

Kelli Benincasa

Encl.

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2015 ELECTRICITY DISTRIBUTION RATES
(Z-factor)

Veridian Connections Inc.

EB-2014-0272

November 14, 2014

Board Staff Submission
Veridian Connections Inc.
2015 Z-factor Distribution Rate Application
EB-2014-0272

Introduction

Veridian Connections Inc. ("Veridian") filed an application with the Ontario Energy Board seeking approval for the recovery of certain amounts related to the restoration of electricity service in the areas of Ajax, Pickering, Clarington and Port Hope due to an ice storm in December 2013.

Board staff has reviewed Veridian's application and its responses to interrogatories, based on which its submissions are set out below.

On December 21st and 22nd an ice storm swept across Southern and Eastern Ontario bringing down trees and power lines. Veridian had approximately 42,000 customers, almost 36% of its customer base, without power at the height of the ice storm. To aid in restoring power, Veridian enacted the Mutual Assistance Plan and obtained the assistance of contracting staff.

On May 2, 2014 Veridian sent a letter to the Board notifying the Board of the infrastructure damage caused by the ice storm and Veridian's intention to file a Z-factor claim.

In this Application, Veridian requested the recovery of a Z-factor claim in the amount of $718,055 as incremental OM&A costs, not including carrying charges. Veridian has not included its internal costs related to labour, material and vehicles of $451,702. Veridian is requesting that the amount be recovered by means of a fixed rate rider across all customer classes based on Veridian's 2014 Board approved Forecast Average number of customers/connections, for a period of 24 months beginning May 1, 2015 and ending April 30, 2017.

A detailed breakdown of the expenses to be recovered is as follows:

Description		
Electricity Distributors	$	112,346
External Contractors	$	462,676
Accommodation and Meals	$	38,028
Vehicle	$	73,319
Communication	$	20,616
Miscellaneous	$	11,071
Projected carrying charges	$	13,980
Z-Factor Amount Requested for Recovery	**$**	**732,035**

Based on the *Board's Report on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors*[1] dated July 14, 2008, Z-factors are intended to provide for unforeseen events outside of a distributor's management control. The cost to the distributor must be material and its causation clear. In order for amounts to be considered for recovery by way of a Z-factor, the amounts must satisfy the following three eligibility criteria:

- Causation – Amounts should be directly related to the Z-factor event. The amounts must be clearly outside of the base upon which rates were derived.

- Materiality – The amounts must exceed the Board-defined materiality threshold and have a significant influence on the operation of the distributor; otherwise they should be expensed in the normal course and addressed through organizational productivity improvements.

- Prudence – The amounts must have been prudently incurred. This means that the distributor's decision to incur the amounts must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.

[1] http://www.ontarioenergyboard.ca/oeb/_Documents/EB-2007-0673/Report_of_the_Board_3rd_Generation_20080715.pdf

Causation

In its Application and in response to Board staff interrogatories (“BSI”), Veridian has:

- Stated that the December ice storm had unprecedented impacts on its electricity distribution system, and the costs incurred to restore service to customers were significant and unavoidable (Application p.6);

- Stated that the third party costs it is seeking to recover for power line contractors, emergency line clearing contractors, and support from other electricity distributors were directly incurred as a result of this severe ice storm and would not otherwise have been incurred (Application p.8);

- Stated the Operating Maintenance and Administrative costs included the recovery amount of $732,035 are outside of the base upon which its 2013 rates were derived (Application p.17);

- Stated that the remainder of Operating, Maintenance and Administrative costs of $140,773 associated with the December 31, 2013 ice storm but incurred in 2014 will be audited in the months of February and March 2015 at the time of their annual external financial statement audit (BSI #1);

- Provided tables of actual and budgeted Overhead Emergency Power Restoration costs for the period of 2010 to 2013. Stated their actual costs exceeded their amounts funded in rates by $924,349 over this period (BSI#5e);

- Stated that up to the time of the December 21st and 22nd ice storm, actual costs in 2013 exceeded the budget, no remaining budget amounts were available to apply (BSI #5g);

- Stated that the additional internal costs of $451,702 that they are not seeking to recover reduce returns that would otherwise accrue to Veridian's shareholder. This reduced return can be characterized as their shareholder's contribution to restoration costs (BSI #6);

- Confirmed that its achieved regulatory ROE for 2013 reported to the Board was

> 12.39%, and stated however their achieved ROE is not above the approved ROE once it is normalized for a one-time event. Specifically, Veridian noted that, "[t]he reported Return on Equity ("ROE") result of 12.39% is higher than the deemed level of 9.85%. The favourable results over deemed were due largely to the recognition of an unrealized gain on a financial instrument. Once normalized for this non-operating item, Veridian's ROE was 8.1% or 1.77% below the deemed level." (BSI #8a).

Based on the amounts funded through rates and actual costs for addressing emergency distribution system problems from 2010 to 2013 provided by Veridian, Board staff notes that since 2010, Veridian has consistently overspent the amounts embedded in rates. In addition, Board staff notes that Veridian's ROE for the two previous years (2011 and 2012) was in line with the deemed. However, it is Board staff's view that there is insufficient information on the record explaining the one-time event referred to by Veridian that was the driver for the higher than normal earnings for 2013. Board staff suggests Veridian describe in its reply submission the nature of the unrealized gain on the financial instrument referred to by Veridian.

Also, it is not clear whether the unaudited amounts noted above are included in the overall claim. If they are included, Board staff would have no concerns with a small portion of these costs being unaudited. If they are not included, then Board staff suggests that Veridian confirm in its reply submission as to whether it will seek this amount in a future application. Board staff notes that the amount is below Veridian's materiality threshold.

Finally, it is not clear if the internal costs for which Veridian is not seeking approval are incremental to what is in current rates or not. Veridian's statement regarding the impact on the company's return suggests that these costs are incremental to the corresponding budgeted amounts in current rates. For example, they may be overtime costs not forecasted in the preceding cost of service application. Board staff suggests that Veridian confirm this in its reply submission.

Overall, Board staff submits that Veridian has demonstrated that the amounts sought for recovery are directly related to the ice storm and outside of the base upon which Veridian's 2013 rates were set .

Materiality

Board staff notes that the Board's materiality threshold for a Z-factor claim is 0.5% of distribution revenue requirement for a distributor with a distribution revenue requirement greater than $10 million and less than or equal to $200 million.

Veridian noted an approved revenue requirement of $49,930,177 from its 2014 cost-of-service application (EB-2013-0174) and a corresponding materiality threshold of $249,650.

Board staff submits that Veridian's $732,035 total cost claim is material.

Prudence

In its Application and in response to Board staff interrogatories, Veridian has:

- Explained that its retention of six electricity distributors was the result of its formal Mutual Assistance Plan with neighbouring utilities (Application p.4);

- Explained that once Environment Canada issued a special weather warning, they moved to an elevated state of preparedness by notifying on call staff, preparing vehicles and issuing standby notices to other critical staff (Application p.8);

- Explained that it sought support from reputable competent power line and emergency line clearing service providers that were familiar with its service areas, business and safety practices (Application p.9);

- Stated the invoiced costs from LDCs are based on a combination of regular labour rates and premium rates depending on the length of time worked per day and the specific days worked. The rates are based on collective agreements (BSI#3c);

- Stated the invoiced costs for external contractors are based on a combination of regular and premium rates dependent upon the hours and days for which the services were provided (BSI#4);

- Explained that due to the urgency of the situation, the extent of the power outages and the need for additional assistance, there was insufficient time to allow for all regular operating procurement practices such as the issuance of an RFP (BSI#4b).

Board staff appreciates that in situations arising from such extraordinary events, a utility faces limited options in safe and timely power restoration efforts. Board staff does have however one concern with Veridian's claim in terms of prudence. Veridian has not fully explained what the premium rates charged by both the LDCs and the contractors represent. If these rates represent overtime and work done on statutory holidays, then Board staff would have no further concerns.

Subject to the above clarification, Board staff submits that Veridian acted prudently in promptly securing assistance to restore power and did so in a cost-effective way, given the circumstances.

Allocation of Costs and Rate Riders

Veridian has applied for fixed rate riders to recover the total amount of $732,035 including carrying costs over a two-year period commencing May 1, 2015. Rate riders have been calculated based on connections and metered customers using the 2014 Board Approved forecast average number of customers/connections per class (EB-2013-0174).

Veridian noted they propose to recover the ice storm costs by a fixed charge rate rider across all customer classes, based on each class's proportion of 2014 Board Approved Distribution Revenue. Board staff notes that past decisions of the Board have ruled that approved costs should be allocated on the basis of distribution revenue, using the last approved fixed/variable split.

Veridian further noted that it believes that a fixed rate rider is simple, transparent and easy for the customers to understand and calculate the exact amount of recovery they will incur. A combination of volumetric and fixed rate riders is less transparent and costs for each customer are unknown until the end of recovery. Additionally, the costs of restoration of electricity service are not dependent upon a customer's energy consumption or demand and are associated more directly with a customer's connection to their distribution network, rather than their throughput or demand.

Board staff submits that the Board typically allocates distribution costs between classes on the basis of distribution revenue. Accordingly, simplicity would suggest that Veridian would allocate the approved recovery amount related to storm costs to all rate classes on the basis of its last approved distribution revenue. Board staff submitted that this approach was appropriate in the Milton Hydro Z-factor allocation and submits that it may continue to be appropriate in this instance as well. However, should there be evidence on the record regarding the nature of the distribution plant that sustained damage and the kinds of customers affected by the storm that would suggest a different allocation – for instance, by customer count rather than by revenues -- Board staff invites Veridian to highlight it in its reply submission.

Board staff notes in the Milton Hydro Z-factor decision (EB-2014-0162) a fixed rate rider for cost recovery was approved. Board staff submits that the use of fixed rate riders is the fairest and simplest to administer.

Veridian has indicated that its proposed rate riders result in total bill impacts to residential customer of 0.16% and for GS <50kW customers of 0.15%. Given that these impacts are so low, and assuming that a one year recovery period would not lead to significant bill impacts, Board staff does not agree that a recovery period of two years is appropriate. Board staff submits a recovery period of one year is preferred in order to reduce intergenerational equity concerns. Board staff requests Veridian to provide updated calculations to account for a one year disposition.

All of which is respectfully submitted