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Ontario

BY EMAIL

November 20, 2014

Ontario Energy Board
P.O. Box 2319
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2300 Yonge Street
Toronto ON M4P 1E4
Kirsten.Walli@ontarioenergyboard.ca

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Innisfil Hydro Distribution Systems Limited
2015 IRM Distribution Rate Application
Board Staff Submission
Board File No. EB-2014-0086

In accordance with Procedural Order No.3, please find attached the Board Staff Submission in the above proceeding. This document is being forwarded to Innisfil Hydro Distribution Systems Limited and to all other registered parties to this proceeding.

Innisfil Hydro Distribution Systems Limited is reminded that its reply submission is due by December 1, 2014.

Yours truly,

Original Signed By

Birgit Armstrong
Advisor, Electricity Rates & Prices

Encl.

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2015 ELECTRICITY DISTRIBUTION RATES

Innisfil Hydro Distribution Systems Limited

EB-2014-0086

November 20, 2014

Board Staff Submission
Innisfil Hydro Distribution Systems Limited
2015 IRM Rate Application
EB-2014-0086

Introduction

Innisfil Hydro Distribution System Limited ("IHDSL") filed an application (the "Application") with the Ontario Energy Board (the "Board") on August 13, 2014, seeking approval for changes to the distribution rates that IHDSL charges for electricity distribution, to be effective January 1, 2015. The Application is based on the 2015 Price Cap IR option.

Included in the Application is a request for cost recovery of IHDSL's new headquarters through an incremental capital module ("ICM"). As well, IHDSL requests a new deferral account to track lost revenue due to the change in streetlight technology by the Town of Innisfil.

Procedural Order No.1 established procedural steps for interrogatories and responses. A technical conference followed by a settlement conference with respect only to the ICM request was convened on October 23, 2014. On November 12, 2014, IHDSL filed a settlement proposal (the "Settlement Proposal"). The parties to the settlement proposal are IHDSL and the Board-approved intervenors in the proceeding: the Vulnerable Energy Consumers' Coalition, the School Energy Coalition and Energy Probe Research Foundation.

IHDSL filed its Argument in Chief with the Board on November 14, 2014.

This is Board staff's submission on the Application, based on Board staff's review of the evidence and the Settlement Proposal. It is intended to assist the Board in arriving at an informed decision on IHDSL's Application with respect to the issues laid out in the evidence and the Settlement Proposal and in setting just and reasonable rates.

Board staff makes detailed submissions on the following:

1. Settlement Proposal
    - – Incremental Capital Module;

2. Other Matters in the Application:
    - Request for a deferral account to track to the impact of conservation programs for the street lighting customer class;
    - Disposition of Deferral and Variance Accounts as per the *Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report"); and,
    - Revisions to the Rate Generator Model.

1. Settlement Proposal

- **Incremental Capital Module**

Background

In its Application, IHDSL requested an ICM to recover the incremental capital costs of $13,246,704 associated with the construction of a new Administration and Operations Centre at 7251 Yonge Street (the "New Headquarters"), which will be in service by November 2014. IHDSL proposes to recover the costs by means of fixed and variable rate riders, which would be in place until such time that IHDSL files its next rebasing application.

The Settlement Proposal sets out the parties' agreement on the following:

- A change to the amount of capital costs in the ICM from $13,246,704 to $10,896,704 (a reduction of $2,350,000);
- A return of 75% of the capital gains from IHDSL's sale of its existing headquarters to its rate payers; and
- Removal of assets related to IHDSL's existing facility from rate base.

Relative to the Application, as filed, the Settlement Proposal results in a reduction of the incremental revenue requirement for IHDSL in 2015 from $1,076,222 to $845,836 for the agreed upon incremental capital amount. This amount will be further offset by an agreed $252,000 reduction associated with the return of capital gains from the sale of the existing facility.

The *Filing Requirements For Electricity Distribution Rate Applications*, last revised on July 25, 2014 for 2015, Chapter 3 Incentive Regulation, requires that the incremental capital expenditure satisfy the eligibility criteria of materiality, need and prudence in order to be considered for recovery prior to rebasing. Applicants must demonstrate that applied-for amounts exceed the Board-defined materiality threshold, clearly have a significant influence on the operation of the distributor and must be clearly outside of the base upon which rates were derived. In addition, the decision to incur the amounts must represent the most cost-effective option for rate payers.

Submission

Materiality and Need

Board staff has reviewed the Settlement Proposal in the context of a discrete ICM request and the applicable Board policies, relevant Board decisions, and the Board's statutory obligations.

In Appendix B of the Settlement Proposal, IHDSL provided a revised 2015 Incremental Capital Work Form, which calculated a materiality threshold of $2,829,737.

The Settlement Proposal sets out the parties' agreement that IHDSL's existing facility is no longer sufficient due to:

- Accessibility, health and safety issues for IHDSL's customers and staff;
- Environmental concerns caused by extreme weather conditions; and,
- Lack of appropriate space for current staff and future staff growth.

In its Application IHDSL also submitted that its existing headquarters (located at 2073 and 2061 Commerce Park Drive, Innisfil) is not meeting Government Office Space Standards of 250 square foot/person with its current staff complement[1].

Board staff submits that IHDSL has fulfilled the Board's criteria for need and materiality.

Prudence

In Board staff's view, the proposal regarding the recovery of the cost of the New Headquarters presented three main issues: whether the capital cost of the New Headquarters is reasonable; the appropriate treatment of any capital gain from the sale of the existing headquarters, the land value of which had appreciated over time; and

[1] Application, EB-2014-0086 Manager's Summary, p. 44 and Response to IR VEC 2, p 27

how to ensure customers are protected given that IHDSL's New Headquarters provides significantly more space than is required to accommodate its current (and near-future) needs. Board staff submits that the Settlement Proposal adequately addresses these issues and, taken as a whole, provides an appropriate solution to IHDSL's current and future space requirements, and does so at a reasonable cost to IHDSL's customers.

Incremental Capital Costs – 7251 Yonge Street (the New Headquarters)

On the issue of total capital cost, Board staff submits that the revised total capital amount of $10,896,704 is reasonable. Board staff notes that the revised capital amount represents a 21.9% reduction from the applied-for capital amount of $13,246,704. Board staff is of the view that the revised capital cost per square foot is comparable to similar investments by other distributors in recent years, namely Enersource Hydro Missisauga Inc. (EB-2012-0033), PowerStream Inc. (EB-2012-0161) and Waterloo North Hydro Inc. (EB-2010-0144). In response to Board Staff interrogatory #6(b), IHDSL provided the following table for comparison:

Table 3

Industry Comparators for new Builds

	Waterloo North Admin & Operations Year 1	Enersource Admin Year 1	PowerStream Admin Year 1	Innisfil Hydro - Admin Compare Year 1	Innisfil Hydro - Admin Compare Year 10	Innisfil Hydro - Admin & Operations Compare Year 1*	Innisfil Hydro - Admin & Operations Compare Year 10**	Innisfil Hydro - Admin & Operations Compare Year 20
Year	2010	2012		2014	2024	2014	2024	2034
Capital Cost	26.5	20	27.7	7.2	7.2	13.2	13.2	13.2
Square Footage	104,000	79,000	92,000	22,853	22,853	36,175	38,745	41,805
Head Office Employees (proj)	117	150	270	41	67	41	67	89
Gross square feet per employee	889	527	341	557	341	882	578	470
Capital cost per employee	$226,496	$133,333	$102,593	$175,610	$107,463	$321,951	$197,015	$148,315
Capital cost/gross square feet	$255	$253	$301	$315	$315	$365	$341	$316

Admin = administrative building only
Admin & Operations = administrative building plus warehouse, storage yard, garage

*Year 1 Admin & Operations Compare removes leasing square footage of 5630 sq. ft.
**Year 10 Admin & Operations Compare added upper level square footage of 2570 sq. ft.

Board staff notes that the comparison to Enersource's Administration Building is based on Enersource's applied-for capital costs. In its Decision and Order of December 13, 2012 regarding Enersource's 2013 CoS distribution rates, the Board disallowed $2 million, or 10%, of Enersource's applied-for capital cost recovery upon finding that the planned-for space was excessive.

In the technical conference IHDSL noted that following the tender of the project, construction costs increased from $200 to $210 per square foot, as a consequence of market conditions[2]. Board staff submits that the capital costs related to the New Headquarters, following the parties' agreed upon reduction of 21.9%, is reasonable and comparable to the above mentioned distributors. Board staff submits that the presence of inflation in the non-residential construction sector since 2010 should be recognized in any comparative evaluation.

Board staff notes that at the time of rebasing the Board will carry out a prudence review of the actual costs to determine the amounts to be incorporated in rate base.

Capital Gain on Sale – 2073 Commerce Park Drive

For the purpose of settlement, the parties agreed to accept a 75% share (or $252,000) of the net after-tax gains to be refunded to ratepayers in addition to the cost recovery of the New Headquarters. Board staff supports the manner by which ratepayers were ensured a benefit associated with the utility's sale and disposition of its existing headquarters. Board staff agrees that it is reasonable to accept a 75% share of net after-tax capital gains from the sale of the existing headquarters as agreed to by the parties.

Board staff is of the view that the sale of the existing headquarters is directly linked to the construction of the New Headquarters. Board staff notes that if it were not for the new facility, the current facility would continue to be used and useful and therefore ratepayers should share in any gain from its sale.

In the Settlement Proposal, IHDSL provided the following net after-tax capital gain to be realized at the close of the sales agreement for the portion of the existing headquarters at 2073 Commerce Park Drive.

Table 4 – Capital Gain on 2073 Commerce Park Drive

Asset description	**Cost**	**Accum Depre**	**NBV**	**Proceeds**	**Loss(Gain)**	**Tax Effect (Est.)**	**Net P&L Loss (Gain)**
Land - 1905	123,493.01		123,493.01				
Building & Fixtures - 1908	748,392.24	$313,565.68	434,826.56				
Total	**871,885.25**	**313,565.68**	**558,319.57**	**(925,000.00)**	**(366,680.43)**	**30,000.00**	**(336,680.43)**

[2] EB-2014-0086, Technical Conference Transcripts, p. 27

Board staff submits that sharing 75% of the proceeds is a reasonable compromise given the range of findings on similar cases. As noted in the settlement agreement, in the case of Toronto Hydro-Electricity System Limited's case (EB-2009-0139) the Board awarded 100% of the net after-tax gains to rate payers, while in the case of Guelph Hydro (EB-2007-0742) proceeds were equally shared between the shareholder and rate payers. The parties also noted that this allocation is consistent with the treatment of capital gains in the Waterloo North Hydro case (EB-2010-0144).

Incremental Revenues – 7251 Yonge Street

IHDSL reports in its Application that the administrative and operational space at the New Headquarters is in excess of IHDSL's current requirements in order to provide for the future staff growth that it expects over the next 20 years. However, it proposes to help to manage its costs by leasing space to other tenants in the interim. This arrangement will help to offset what must be recovered through rates. There was no adjustment to the ICM to reflect potential near-term leasing revenues. However, the parties agreed that any future leasing revenues will be accounted for, on a prospective basis, at the time of IHDSL's next rebasing application. Board staff notes that this arrangement, which is consistent with Board policy regarding the treatment of other revenues, will help to provide some means of protecting IHDSL's customers from costs associated with surplus space while allowing for future growth.

Incremental Costs – 7251 Yonge Street

As noted in the Settlement Proposal, IHDSL expects to incur incremental OM&A costs related to the New Headquarters. During the technical conference, IHDSL suggested that it track incremental OM&A related to the new facility in a deferral account[3]. For the purpose of settlement, the parties agreed that the scope of an ICM is intended to recover the revenue requirement of the associated capital additions only and, therefore, no DVA to record leasing revenues during IHDSL's IRM term is necessary. Board staff submits that this treatment is symmetrical with the agreed upon exclusion of incremental OM&A costs during the IRM period.

Rate Base Treatment of Net Book Value – 2073 Commerce Park Drive

[3] EB-2014-0086, Technical Conference Transcripts, p. 28, lines 27-28 and p. 29, line 1-10

Board staff agrees that since the New Headquarters is replacing an existing asset that is currently in rate base, the Net Book Value ("NBV") of the existing assets should be removed from rate base effective January 1, 2015. Board staff notes that there is no mechanism during the IRM term to adjust rate base; accordingly, Board staff supports the proposed treatment to calculate the incremental revenue requirement by reducing the NBV of land and building and fixtures of the new facility by the NBV of the existing facility ($124,000 for existing land and $435,000 for buildings and fixtures). Board staff notes that any final adjustments to rate base to reflect the removal of the current facility, and the addition of the new headquarters, including accumulated depreciation, will be made at the time of rebasing.

2. Other Matters in the Application:

- **Request for a Deferral Variance Account (DVA) to track actual relative to forecast revenues for the street light customer class due to change in technology**

Background

IHDSL reported in its application that the Town of Innisfil intends to convert all existing street lights to LED technology by December 31, 2014. Innisfil Hydro accordingly requested approval to establish a Variance Account to track the difference between forecasted and actual revenues from the Street Lighting rate class until IHDSL's next rebasing application, expected in time for January 1, 2017 rates.

For the Street Lighting rate class, IHDSL submitted that actual reductions due to CDM will exceed the CDM impact included in its load forecast. IHDSL also submitted that the resulting lost revenues from the Street Lighting rate class will persist until IHDSL applies for new rates as part of its 2017 cost of service application.

IHDSL requested that "the Board establish a mechanism to align the CDM adjustment included in its load forecast and scenarios in which specific rate classes over exceed forecasted CDM impacts". IHDSL noted that by tracking actual revenues compared to the approved forecast of the Street Lighting rate class, it will have a documented baseline to be used at its next rebasing application.

Submission

Board staff does not support IHDSL's request to establish a new variance account to record and track various data points related to its Street Lighting rate class. The Board already has the lost revenue adjustment mechanism variance account to manage the difference between forecast and actual CDM results. As outlined in the Board's CDM Guidelines issued on April 26, 2012 (the "2012 CDM Guidelines), Account 1568 – LRAMVA was established to ensure distributors were held revenue-neutral with respect to lost revenues that resulted from implementing approved CDM programs between 2011 and 2014. The development of Account 1568 - LRAMVA was consistent with the CDM Directive issued by the Minister of Energy and Infrastructure to the Board on March 31, 2010 ("2010 CDM Directive"). Section 12 of the 2010 CDM Directive noted that "the Board shall have regard to the objective that lost revenues that result from CDM Programs should not act as a disincentive to a distributor."

On March 31, 2014, the Minister of Energy issued a new directive to the Board for the period from 2015 to 2020 that contains very similar wording and must be addressed by January 1, 2015. Board staff submits that it can be reasonably expected that additional guidance from the Board will be provided in response to the 2014 Conservation Directive before the end of 2014.

Board staff anticipates that any forthcoming guidance from the Board on conservation matters will address the manner by which lost revenue due to conservation are to be managed. Board staff also expects that the effectiveness dates of the Board's guidance will accommodate the timing that is an issue for the applicant.

Finally, Board staff notes that nothing precludes the distributor from tracking information on its own to be used at the time of its next rebasing.

- **Disposition of DVAs as per the EDDVAR Report**

Background

IHDSL completed the DVA continuity schedule included in the 2015 IRM Rate Generator Model at Tab 5 for its Group 1 DVAs. In response to Board Staff interrogatory No.1(b), IHDSL submitted that originally-filed balances for Account 1595 included amounts which are already being recovered through rate riders until April 30, 2014[4]. Consequently, IHDSL revised its continuity schedule to update the balances in Account 1595 to exclude these amounts from the proposed disposition.

IHDSL's total Group 1 DVA balances amount to a debit of $1,274,655. The balance of Account 1589 – Global Adjustment Sub-Account is a debit of $678,344, and is applicable only to Non-RPP customers. These balances also include interest calculated to December 31, 2014. Based on the threshold test calculation, the Group 1 DVA balances equate to $0.0055 per kWh. This amount exceeds the pre-set disposition threshold. IHDSL requested disposition of the Group 1 DVA balances over a one-year period.

Submission

Board staff submits that the updates to the balance in Accounts 1595 (2012) and 1595 (2013) are appropriate. Per the Electricity Distributor's Deferral and Variance Account Review Initiative ("EDDVAR Report") dated July 31, 2009, the balances to be reviewed in the distributor's application will be the most recent audited balances ending December 31 as reported to the Board as of April 30 through the *Reporting and Record-keeping Requirements*. In IHDSL's case, this would be for balances as at December 31, 2013. Balances in 2014 would persist until December 31, 2014 and be disposed in the 2016 IRM application. Board staff agrees that the rate riders for disposition of DVAs (2012) and (2013) are effective until April 30, 2014 and should not be reflected in the disposition of Account 1595 until the time when the year end balances in these accounts have been audited.

Board staff has reviewed IHDSL's Group 1 DVA balances and notes that the principal balances as of December 31, 2013 reconcile with the balances reported as part of the *Reporting and Record-keeping Requirements*.

Board staff supports IHDSL's proposal to dispose of its DVA balances over the requested one-year period, consistent with the default period identified in the EDDVAR Report.

- **Revisions to the Rate Generator Model**

[4] Interrogatory Responses, October 16, 2014, OEB Staff-IR 1, p. 3

In the interrogatory phase, Board staff noted that IHDSL entered the incorrect Hydro One Sub-Transmission Rates as well as incorrect amounts for Rate Rider #9A in the input cells on tab 15 of the Rate Generator Model. In its responses, IHDSL acknowledged the error and requested that staff make the necessary corrections to the model.

Board staff further notes that IHDSL entered incorrect billing determinants in tab 14 of the Rate Generator Model. In response IHDSL acknowledged the error and provided an updated Rate Generator Model.

Board staff notes that the billing determinants provided in tab 14 of the updated Rate Generator do not reconcile to IHDSL's RRR 2.1.5 consumption data. Board staff notes that the following data has been filed by IHDSL in its RRR filing:

Table 1: RTSR Billing determinants as filed vs. RRR data

Rate Class	**Updated Rate Generator kWh**	**RRR data as filed kWh**
Residential	138,438,121	149,683,526
GS<50 kW	25,862,697	31,141,868
GS>50 kW GS>50 kW (Interval metered)	15,564,152 28,904,853	50,837,709
Street Light	1,483,729	1,495,302
Sentinel Light	97,543	108,390
USL	442,488	474,042

Pursuant to the Board's Guideline G-2008-0001, Board staff notes that the Board will update the applicable data at the time of the Board's Decision on the Application based on the Uniform Transmission Rates in place at that time. Attached to this submission is a partially updated Rate Generator model; and, Board staff requests that IHDSL review the revised model and provide updated amounts for tab 14 in IHDSL's reply submission.

All of which is respectfully submitted