2015 ELECTRICITY DISTRIBUTION RATES

Niagara Peninsula Energy Inc.

EB-2014-0096

STAFF SUBMISSION

March 27, 2015

INTRODUCTION

Niagara Peninsula Energy Inc. ("NPEI") filed an application with the Ontario Energy Board (OEB) on September 23, 2014 seeking approval for changes to its electricity distribution rates, to be effective May 1, 2015.

The OEB held a technical conference on January 20, 2015 and a settlement conference on February 3 and 4, 2015.

NPEI and the intervenors filed a settlement proposal, representing a partial settlement, on February 25, 2015.

On March 4, 2015 OEB staff submitted that parties to the settlement proposal had considered the settled issues within the context of the Renewed Regulatory Framework for Electricity, and that the OEB's approval of the proposal as filed would adequately reflect the public interest and would result in just and reasonable rates for customers.

The following issues remained unsettled:

- The appropriate percentage factor to be used to calculate NPEI's Working Capital Allowance component of rate base, including the impact of the merger on the Working Capital Allowance reflected in the Revenue Requirement; and

- The appropriate fixed/variable spilt for the residential class.

The OEB held an oral hearing to hear the unsettled issues on March 17, 2015. At the outset of the oral hearing, the OEB accepted the settlement proposal as filed, subject to certain wording changes regarding the future treatment of the applicant's proposed acquisition of certain Niagara Parks Commission assets (under section 5.1) and a revision of the bill impact percentages (under section 3.3). In this regard, NPEI and the intervenors filed an amended settlement proposal dated March 25, 2015.

The following are OEB staff's submissions on the unsettled issues.

Working Capital Allowance

NPEI is proposing a working capital allowance (WCA) factor of 13%. Intervenors' cross-examination of the applicant on this issue indicates that they question the appropriateness of this number.

In its letter to distributors of April 12, 2012 (OEB letter), the OEB updated its filing requirements to establish its approach to the calculation of WCA for LDCs for 2013 cost of service applications. That approach, which continues to be in place in the 2014 edition of the filing requirements, allows applicants to calculate their WCA either on the basis of the OEB's 13% allowance approach or by filing a lead/lag study. The only exception to this approach is if the applicant has been previously directed by the OEB to undertake a lead lag study on which its current WCA is based. Under those circumstances, an applicant proposing a revision to its WCA must file an updated study in support of its proposal.

Under the 13% allowance approach, a distributor calculates its WCA on the basis of 13% of the sum of controllable expenses and a forecast of the cost of power, taking into account the proportion of consumption that is subject to the regulated price plan, among other factors.[1]

Prior to the issuance of the OEB's letter, the OEB's default WCA factor had been 15%. The OEB is currently examining its approach to WCA as part of its *Review of Electricity and Natural Gas Distributors' Residential Customer Billing Practices and Performance*, which is intended to examine factors beyond the impact of monthly billing on WCA.

NPEI has filed its WCA on the basis of the 13% allowance approach. Based on the load forecast and other elements that were agreed in the settlement proposal, NPEI proposes a WCA of $20,874,706   included in its rate base.

Prior to the merger of Peninsula West Utilities and Niagara Falls Hydro, the Peninsula West Utilities customers were billed monthly and Niagara Falls Hydro converted its residential and several GS >50 kW customers to monthly billing in May 2010.[2]

[1] Filing Requirements for Electricity Distribution Rate Applications, July 18, 2014, Chapter 2, s. 2.5.1.3, page 19

[2] Exhibit K1.3 page 11 of 18.

NPEI has not completed a lead/lag study. It has neither been directed to do so by the OEB [3], nor has it attempted to benchmark its working capital requirements to those of other distributors that had filed lead lag studies.[4]

As stated in the OEB's Letter, the OEB's consideration of an appropriate default value for calculating WCA in the absence of a lead/lag study was based on a review of lead/lag studies filed in cost of service applications in the few years leading up to the issuance of the letter.

Energy Probe filed a compendium at Exhibit K1.3 which contains lead/lag studies for Toronto Hydro, Hydro One Distribution, Horizon Utilities and Hydro Ottawa.

LATEST WORKING CAPITAL FILINGS

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

(1) EB-2011-0054 INTERROGATORY RESPONSE - EX. K2, ISSUE 2.2, INTERROGATORY #2
(2) EB-2014-0002 INTERROGATORY RESPONSE - 2-ENERGY PROBE-11

As to whether it would be appropriate to use default value, 13%, for the working capital allowance that is higher those resulting from lead-lag studies, NPEI indicated that without a lead-lag study the specifics circumstances for a utility are unknown.

The OEB has in the past found it to be inappropriate to adopt the results of a lead/lag study from one utility to apply to another utility without a thorough analysis concluding that the utilities are comparable. Most recently, in a Motion to Review and Vary by the School Energy Coalition for a review of the OEB's Decision and Order in proceeding EB-2013-0147, the OEB stated:

[3] EB-2014-0096, Oral Hearing Transcript vol. 1, page 22.
[4] Ibid page 36.

> The OEB finds that using a consistent WCA default value in cases where lead/lag studies have not been conducted to be a better approach than attempting to use simplified methods to derive a utility-specific WCA value for each case from other lead/lag studies which may not reflect the unique circumstances of such utility[5].

Submission

OEB staff submits that NPEI has calculated its WCA in accordance with the OEB's policies, and that there is no evidence in this proceeding that would allow for specific reductions in the WCA factor to be directly applied to NPEI.

As illustrated in Exhibit K1.3, clearly there is a wide range among LDCs in the revenue lags and expense leads that are calculated within the individual lead/lag studies filed to date. OEB staff does not see merit in applying the full results of one study to any one utility. Given the uncertainty on the implications to NPEI of various factors, it is reasonable for the OEB to approve the WCA based on the OEB's policy of 13%. The intervenors have raised a number of points that should be taken into consideration by the OEB in its future review of the WCA policy.

OEB staff notes that the settlement proposal indicates that NPEI, regardless of the OEB's decision on the appropriate percentage, will undertake a lead/lag study prior to next cost of service rate application, unless the OEB completes a generic hearing that is determinative of this issue prior to that time.[6]

<u>Fixed/Variable Split</u>

NPEI originally proposed a 65%/35% fixed/variable split for its residential customer class. The existing fixed /variable split is 58.53%/41.47%.

Subsequent to the oral hearing at which NPEI's proposal was discussed, NPEI provided undertaking J1.1, in which it confirmed that 711 kWh was the minimum consumption level at which a residential customer would start paying less under a 65/35% fixed-variable split. NPEI further indicated that it was no longer proposing to move from its existing fixed/variable split percentage to 65%/35%, because a 711kWh cross-over point would mean that only 40% of residential customers would benefit from the change.

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[5] EB-2013-0147/EB-2014-0055, Decision and Order, October 23, 2014, page 4
[6] EB-2014-0096 Amended Settlement Proposal ,dated March 25, 2015, p. 12/37

Submission

OEB staff notes that the OEB "believes that a fixed rate design for recovery of electricity distribution costs is the most effective rate design for ensuring that rates reflect the cost drivers for the distribution system"[7], particularly for low volume residential customers. OEB staff submits that an increase in fixed costs for the residential customer class would be directionally appropriate with OEB guidance to date. Nevertheless, staff acknowledges that further information on the timing and pace of the adoption of fixed rates is still forthcoming, and that the policies applicable to distributors filing for 2015 rates are those enumerated in the OEB's filing requirements.

Accordingly, OEB staff notes that NPEI's proposed fixed rate that corresponds to the existing fixed/variable split is $16.06 and is less than the Customer Unit Cost per month - Minimum System with PLCC Adjustment.

Residential[8]

Customer Unit Cost per month - Avoided Cost	$6.67
Customer Unit Cost per month - Directly Related	$9.19
Customer Unit Cost per month - Minimum System with PLCC Adjustment	$27.89
Existing Approved Fixed Charge	$16.06

Board staff submits that NPEI's maintenance of the status quo is consistent with the Section 2.11.1 of the 2015 Filing Requirements and on this basis it should be accepted by the OEB.

All of which is respectfully submitted.

[7] Draft Report of the Board: Rate Design for Electricity Distributors. EB-2012-0410, March 31, 2014, p1.
[8] Source: Cost Allocation Model (excel) filed with the Settlement Proposal dated March February 25, 2015