March 26, 2015

BY FAX & BY COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St, Suite 2701
Toronto ON M4P 1E4

Dear Ms. Walli:

Board File No. EB-2014-0096
Niagara Peninsula Energy Inc. --- 2015 Cost of Service
Energy Probe – Argument

Pursuant to the Oral Hearing, March 17, 2015, please find attached the Argument of Energy Probe Research Foundation (Energy Probe) in the EB-2014-0096 proceeding for consideration of the Board.

Should you require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh
Case Manager

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EB-2014-0096

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 Niagara Peninsula Energy Inc. for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2015.

ENERGY PROBE RESEARCH FOUNDATION
("ENERGY PROBE")

ARGUMENT

March 26, 2015

NIAGARA PENINSULA ENERGY INC.
2015 RATES APPLICATION

EB-2014-0096

ARGUMENT OF ENERGY PROBE RESEARCH FOUNDATION

A- INTRODUCTION

Niagara Peninsula Energy Inc. ("NPEI") filed a Settlement Proposal in this proceeding with the Board on February 25, 2015. The Board indicated during the oral hearing that it was prepared to accept the Settlement Proposal when it was refiled with some agreed to wording changes (Tr. Vol. 1, page 73). The Amended Settlement Proposal reflecting these wording changes was refiled with the Board on March 24, 2015.

This is the Argument of the Energy Probe Research Foundation ("Energy Probe") related to the unsettled issues in this proceeding. These two unsettled issues - the working capital allowance percentage and the fixed variable split for residential customers are dealt with below in the Submissions section of this argument and follow the Issues List as approved by the Board in the Issues List Decision dated January 29, 2015.

Energy Probe further notes that a number of issues shown in the Settlement Proposal are shown as a Partial Settlement. Energy Probe is not making any submission on these issues as it notes that these issues are settled with the exception that they may be impacted by the Board's decision with respect to the two unsettled issues noted above.

Energy Probe has structured its submissions based on the Report of the Board - Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach dated October 18, 2012 ("RRFE"), in which it is stated 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 to be on results rather than activities and will better respond to customer preferences.

B - SUBMISSIONS

ISSUE 1.1

Is the level of planned capital expenditures appropriate and is the rationale for planning and pacing choices appropriate and adequately explained, giving due consideration to:

- **customer feedback and preferences;**
- **productivity;**
- **benchmarking of costs;**
- **reliability and service quality;**
- **impact on distribution rates;**
- **trade-offs with OM&A spending;**
- **government-mandated obligations; and**
- **the objectives of the Applicant and its customers?**

Under this issue Energy Probe deals solely with the working capital allowance ("WCA") proposal to use the default percentage provided in the guidelines.

Energy Probe submits that a 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. The 13% does not reflect the RRFE and does not give due consideration to customer feedback and preferences, benchmarking of costs, impact on distribution rates, trade-offs with OM&A spending and the objectives of the Applicant and its customers, all of which are noted above as part of this issue.

Furthermore, the 13% cannot be considered reasonable when the distributor itself has provided evidence of the reduction in its historical cash flow requirements that it has **not** reflected in the current application.

a) The NPEI Situation

Energy Probe submits that NPEI is in a unique situation with respect to the working capital allowance percentage. Since its last cost of service rebasing application, it has converted more than half of its customers from bi-monthly to monthly billing (Tr. Vol. 1, page 43). NPEI has reflected the incremental OM&A costs associated with change, along with some of the cost reductions (Tr. Vol. 1, page 42). However, NPEI has not undertaken lead/lag study to reflect the reduction in the working capital requirement.

When asked why NPEI did not do a lead/lag study, or benchmark its working capital allowance requirements to those distributors that have done such studies, Ms. Wilson stated (Tr. Vol. 1, page 36):

> *"Well, I wasn't required to do a lead lag study, so I didn't benchmark to anybody else. I followed the guidelines."*

With all due respect, Energy Probe submits that "following the guidelines" is not an acceptable alternative for a distributor that has changed the billing frequency for more than half of its customers and included the incremental costs of this change in rates.

Rather, the onus is on the applicant to support its cost of service, including the costs associated with its working capital requirements. By failing to provide a lead/lag study that reflected the changes made by the utility from its previous cost of service application, NPEI has failed to meet this onus.

However, Energy Probe submits that NPEI has provided sufficient evidence from which the Board can determine an appropriate level of the WCA percentage.

As shown on page 18 of Exhibit K1.3, the approved level of the working capital allowance was $18,437,623. This was based on the use of the 15% WCA percentage in the EB-2010-0138 case for 2011 rates.

In the April 12, 2012 letter (noted below), the Board reduced the 15% to 13% based on its determination that it was not appropriate for a default value for WCA to be set at a higher level than those resulting from lead/lag studies which it had reviewed.

Based on this change from 15% to 13%, Energy Probe submits that the working capital allowance approved in EB-2010-0138 would have been $15,979,274 based on the use of the 13% factor.

This change, however, still does not reflect the impact of moving more than half of the customers to monthly billing. NPEI has, however, provided evidence as to what that impact was. In particular, the response to an interrogatory in EB-2010-0138, which is found at pages 11 through 16 of Exhibit K1.3, provides this information. To be specific, Appendix E to the response indicates that there was a forecasted reduction in working capital requirements of $3 million.

This reduction of $3 million in working capital requirements is independent of whether the WCA allowance was calculated using 13% or 15% for regulatory purposes. The NPEI witness agreed that this was the case (Tr. Vol. 1, page 43-44).

Ms. Wilson testified that NPEI's working capital requirements were basically unchanged as a result of the $3 million reduction noted above being offset by increase in the cost of power (Tr. Vol. 1, pages 44-45). In other words, the $15,979,274 working capital requirement calculated using the EB-2010-0138 figures and the 13% factor would have decreased by about $3 million due to the move to monthly billing and would have increased by roughly the same amount due to the higher cost of power. What that means is that a working capital requirement of about $16 million is appropriate, given the evidence of the applicant. Based on a total cost of power and controllable expense of $160,574,664 shown in the RRWF attached to the Settlement Proposal, this approximate $16 million requirement is equivalent to a WCA percentage of 9.95%.

Energy Probe notes that Ms. Wilson indicated that the working capital requirements of NPEI were impacted by the loss of the water billing. As the Board is aware, the working capital allowance is based solely on the cost of power and controllable expenses which are related to the provision of electricity distribution services. The fact that NPEI may have had additional cash on hand when it provided water billing services has no impact on the working capital requirement of the regulated utility.

Similarly, Ms. Wilson talked about three $10 million loans that the utility had to take out over the past number of years. It was clear in her description of this to Mr. Shepherd (Tr. Vol. 1, pages 64-67) that this additional money was to run the business. It was, in part to replace the cash balance that was associated with water billing, but it was also to finance growth in rate base. Again, these loans are not relevant to the issue of the working capital requirement. Ratepayers are paying for this additional debt in their rates.

Energy Probe submits that the most telling aspect of NPEI's failure to reflect the impact of the reduction in the working capital requirement is the following statement of Ms. Wilson (Tr. Vol. 1, page 67):

> *"I estimated this from a cost benefit perspective of taking it to the board.* ***It would be beneficial to our customers*** *that they would be able to see their usage on a much more timely basis,* ***and there was a positive benefit****. This was not used for the purpose of calculating a working capital allowance or the preparation of the 2011 rate application,* ***it was a memo that was provided for the purpose of telling our board of directors there is a cost benefit due -- the cost on that time was positive to move forward*** *with monthly billing."* (emphasis added)

Clearly, NPEI had identified that there was a positive impact on the costs to serve customers. The cost increases were more than offset by the cost decreases, which included a lowering of the working capital requirement. Energy Probe agrees with this. What Energy Probe does not agree with, and which the Board should not condone, is keeping part of the benefits for the shareholder rather than passing them on to the customers. If the Board does not require a distributor to pass on savings to customers, while allowing them to pass on incremental costs for the same thing, then phrases such as customer engagement, customer focus, value for money and focus on outcomes within the context of the RRFE are meaningless.

Finally, Energy Probes notes that NPEI has agreed to undertake a lead/lag study prior to its next cost of service proceeding, unless the Board completes a generic hearing that is determinative of this issue prior to that time. Energy Probe supports the need for a lead/lag study, but does not support customers having to wait for 5 years to have the results reflected in rates. Such a delay certainly does not reflect any customer engagement, customer focus or value for money. NPEI's own evidence supports a working capital allowance percentage of just under 10%.

b) The RRFE and Board Guidelines

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:

> *"...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 1 below. A review of all applications and decisions prior to April 12, 2012 indicates that these were the only lead-lag studies that were filed by electricity distributors. These four studies are shown in Table 1 below.

As shown in Table 1 the average of the Board 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 acknowledged 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.

Table 1

FILE NO.	DISTRIBUTOR	BOARD APPROVED	SERVICE LAG	CHANGE IN SERVICE LAG	% CHANGE IN SERVICE LAG	WCA IF BILLED MONTHLY	
(a)	(b)	(c)	(d)	(e) = 15.21-(d)	(f) = (e)/365	(g) = (c) + (f)	
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	14.20%	30.24	NA	NA	9.60%	(5)
AVERAGE		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)

ii) Fact - The 13% is Wrong for Monthly Billing

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 1 by looking at the Service Lag column. If a distributor billed all 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 1, 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 the 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."*

The Board emphasized this benefit in the Notice of Proposal - Proposed Amendments to the Distribution System Code (EB-2014-0198) dated February 5, 2014 in which it stated that it acknowledged that incremental costs associated with monthly billing (page 5) and that *"The Board expects that these costs may be mitigated by improved cash flows for distributors as a result of monthly billing.."*. Clearly the Board recognizes that monthly billing results in lower working capital requirements than does bi-monthly billing.

NPEI currently bills all of its customers on a monthly basis and has done so since 2010. 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 distributor that bills all customers monthly is not appropriate. It is no more appropriate than a distributor forecasting tree trimming costs based on a 3 year cycle when it is clear that the distributor is actually on a 6 year cycle.

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 for the Board to approve the results from the average of a number of lead-lag studies where the utilities included in that average are demonstrably different from NPEI. 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 1 above, 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 each of the four lead-lag studies shown in Table 1.

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 (Interrogatory 2-Staff-23):

> ***"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 an "obsolete methodology" in reference to the use of customer weighting method for revenue lags. 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 and cannot 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 obviously 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 re-calculate the average percentage WCA based on a service lag of 15.21 days that represents the fact that NPEI 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 NPEI witnesses agreed that none of the other components of the working capital allowance changed when they moved all customers to monthly billing (Tr. Vol. 1, pages 38-40). In other words, changes to the service lag to reflect billing frequency do not have any impact on the other components of the WCA calculation.

Energy Probe further submits 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 NPEI 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 are based on monthly billing.

Table 1 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 and continues to be based on the four original lead/lag filings.

Table 1 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 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%.

iv) The Correct Approach Extended

Energy Probe notes that a number of more recent lead-lag studies have been filed and/or approved by the Board since the original four studies used by the Board to set the 13% figure. A summary of these studies are found in Exhibit K1.3 at page 17. 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 to be reviewed by the Board. It also includes studies by three additional distributors: Enersource, London Hydro and Veridian.

Energy Probe submits that the Board should use the most recent studies available to determine an appropriate figure for NPEI. This would be consistent with the Board's April 12, 2012 letter in which *"The Board 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"*. Nothing has changed, except the Board now has more lead/lag studies.

Energy Probe further notes that the list provided in Table 2 below 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 1 and extending it to the larger group of studies included in Exhibit K1.3, Energy Probe has converted the figures 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 list bills on a monthly basis. As can be seen in the Service Lag column of Table 2, 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 2 below.

Some 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.

Table 2

FILE NO.	DISTRIBUTOR	APPLIED OR APPROVED	SERVICE LAG	CHANGE IN SERVICE LAG (e) = 15.21-(d)	% CHANGE IN SERVICE LAG	WCA IF BILLED MONTHLY	
(a)	(b)	(c)	(d)	(d)	(f) = (e)/365	(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%	
		11.42%	22.38			9.30%	

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

Table 2 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 1 earlier, Energy Probe submits that by standardizing the results to reflect monthly billing reduces the variance or volatility in the WCA percentages. The WCA percentages range from 7.4% to 14.2%, for a range of 6.80 percentage points, 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 percentage points 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 1.

Table 2 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 and up-to-date and, of course, correct. 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, which is a component of the cost of service, is provided in order to allow a distributor to recover its costs associated with the financing it requires in order to manage 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 1 and 2 above, a more appropriate benchmark of 9.3% to 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 in the 9.3% to 9.5% range.

vi) 13% Default Conflicts with RRFE

Energy Probe submits that the 13% default in the filing guidelines is not compatible with the RRFE. Nor does it satisfy each of the sub-issues under Issue 1.1.

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. This was confirmed in the NPEI customer survey provided in Exhibit 1, Tab 3, Schedule 1, Attachment 4.

As noted during cross-examination, the impact of a one percentage point reduction in the WCA percentage results in a reduction of $117,934 in costs to ratepayers (Undertaking J1.2 and Tr. Vol. 1, page 40). Reducing the WCA from 13% to 9.5% would, therefore, result in a reduction of more than $410,000 in rates. This reduction represents a significant portion of the base revenue requirement, which is $28,665,192, as shown in the RRWF attached to the Settlement Proposal in the Settlement Agreement column. Put another way, the reduction in the working capital allowance of $410,000 represents more than 1.4% of the base revenue requirement and would result in an average reduction in rates of the same 1.4%.

Based on the 13% proposed by NPEI, this amounts to about $1,375,000, or nearly 5% of the base revenue requirement shown in the RRWF attached to the Settlement Proposal. 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. The outcome that is being proposed by NPEI 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 NPEI. The Board recognizes that this is an additional benefit associated with monthly billing in the Billing Practices Report and in the corresponding Notice of Proposal, both 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 NPEI that now bills monthly.

Energy Probe submits that the improved cash flow is just not an additional benefit, it is one of the largest benefits 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).

NPEI's own evidence backs up this statement. As shown in Appendix E and F to the interrogatory response filed in EB-2010-0138 and included at pages 11 through 16 in Exhibit K1.3, the reduction in interest expense due to the reduction in the working capital requirement represents somewhere in the neighbourhood of 70% to 90% of the net savings.

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 for ratepayers under the RRFE that should, and can, be corrected.

With regards to customer preferences, Energy Probe submits 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 NPEI are not being passed on to ratepayers, as they ought to be.

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.

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.

The use of the default value results in ignoring customer preferences (monthly billing but will all savings passed through to customers, not just incremental costs), ignoring benchmarks that are available for the Board to take into consideration, ignoring the significant and unjustified impact on distribution rates, does not fully take into account the trade-offs with OM&A spending related to monthly billing, and ignores the objectives of its customers (lower costs).

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.

c) Summary and Recommendations

Energy Probe submits that the Board cannot rely on the default 13% for setting rates for NPEI. It has been clearly demonstrated that this figure is based on an obsolete methodology that is out-of-date. NPEI's own evidence does not support at figure of 13%.

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 NPEI now does. This reflects proper benchmarking, a hallmark of the RRFE.

Based on the calculations in Tables 1 and 2 which provide an apples to apples (or in this instance, monthly billing to monthly billing) comparison in part (b), along with the specific circumstances for NPEI discussed in section (a) above, Energy Probe submits that the Board should direct NPEI to use a WCA percentage in the range of 9.5% to 10.0%.

Use of a 9.5% to 10.0% WCA will reduce rates by $350,000 to $410,000 a year. Over the term of the IRM plan, this will result in savings to ratepayers of $1.75 million to more than $2 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 cannot 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 1.2% to 1.4%, Energy Probe submits that if the Board approves a 13% WCA for the 2015 test year, it should direct NPEI 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 NPEI to continue to pay $350,000 to $410,000 a year, or 1.2% to 1.4% of their distribution bill, because NPEI 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 NPEI uses and that ratepayers pay for, and was not supported by their own evidence.

Finally, Energy Probe notes that in the April 12, 2012 letter the Board stated:

> *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."*

As illustrated in Table 2 above, based on all of the updated or new lead/lag studies provided since this letter was issued and with the adjustment to reflect monthly billing, no lead/lag study has come anywhere near 13%. The average is 9.30%. The best in class is near 7.0%. Based on their own evidence, nothing above 10% has been justified.

The Board should not compromise its principles (as outlined in the April 12, 2012 letter) for the sake of a guideline. Ratepayers deserve better from this Board.

ISSUE 3.3.1

Are the applicant's proposals regarding its fixed/variable ratios appropriate?

NPEI had proposed to increase the fixed-variable split to 65/35 from the status quo ratio of approximately 58/42.

Mr. Stoll indicated that the actual cross over point where customers would be better off or worse off was 711 kWh per month and that NPEI would provide the number of customers that would be better off (Tr. Vol. 1, page 75).

As Mr. Stoll noted in his argument-in-chief (Tr. Vol. 1, page 76), one of the principles for this change as proposed by NPEI was that it was felt that the change would benefit the greatest number of customers. Moreover, Mr. Stoll stressed that that this point would actually be confirmed through the answer to the undertaking.

The NPEI witnesses repeated stressed that about two thirds of the residential customers would benefit from this increase in the fixed variable ratio and that was why NPEI had proposed it (Tr. Vol. 1, pages 24, 51, 57 & 58).

However, as shown in the response to Undertaking J1.1, NPEI has determined that only about 40% of its residential customers would benefit from the proposed shift to a 65/35 fixed-variable split. As a result, NPEI has indicated that it is revising its request and proposes to maintain the current fixed-variable split for the residential class, in order to provide a benefit to the greatest number of customers.

Energy Probe supports the revised NPEI proposal to maintain the current fixed-variable split for the residential customers.

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

March 26, 2015

Randy Aiken
Consultant to Energy Probe