

**2015 & 2016 REVENUE REQUIREMENT AND  
CUSTOMER DELIVERY POINT PERFORMANCE  
STANDARDS**

**Canadian Niagara Power Inc.-Transmission**

**EB-2014-0204**

**STAFF SUBMISSION**

**March 30, 2015**

## INTRODUCTION

Canadian Niagara Power Inc. (CNPI Tx) filed a complete cost of service application with the Ontario Energy Board (OEB) on November 17, 2014 under section 78 of the Ontario Energy Board Act, 1998, S.O. 1998, c. 15, (Schedule B), seeking approval for changes to its electricity transmission revenue requirements for 2015 and 2016 to be effective January 1, 2015 and January 1, 2016. In the same proceeding, CNPI Tx has also filed for approval of its customer delivery point performance standards. CNPI Tx recovers its OEB-approved revenue requirement through Ontario's Uniform Transmission Rates.

The only intervenor in this proceeding, the Independent Electricity System Operator, did not actively participate.

CNPI Tx originally requested specific approval of the following:

- Approval of a revenue requirement of \$4,530,710 and \$4,818,057 for the 2015 test year and the 2016 test year, respectively
- Approval of operating costs of \$2,968,381 and \$3,072,214 for the 2015 test year and the 2016 test year, respectively
- Approval of capital expenditures of \$5,852,942 and \$740,000 for the 2015 test year and the 2016 test year, respectively
- An update to the uniform transmission rates to allow recovery of the proposed revenue requirements for 2015 and 2016, effective January 1 of each of these test years
- Approval of its customer delivery point performance standards

The OEB conducted an oral hearing on the application on March 12, 2015. CNPI Tx filed its argument-in-chief, which outlined the application as currently understood, on March 19, 2015.

CNPI Tx in its argument-in-chief revised some aspects of its application as originally filed. The revisions are as follows:

- A revenue requirement of \$4,467,388 for the 2015 test year <sup>1</sup>
- A revenue requirement of \$4,843,623 for the 2016 test year <sup>2</sup>

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<sup>1</sup> Adjusted original revenue requirement to reflect correction to an OEB staff identified error regarding rate base, continuing staff vacancies and a property tax increase.

<sup>2</sup> Adjusted original revenue requirement to reflect correction to an OEB staff identified error regarding rate base and a property tax increase.

The OEB did not create an issues list for this application. OEB staff has reviewed the application, including interrogatories, undertakings and oral examination, and this submission will solely focus on matters in the application which OEB staff feel are of concern. On this basis, unless indicated otherwise in this submission, OEB staff supports the requests presented in CNPI Tx's application and as revised in CNPI Tx's argument -in-chief.

### **Updated Revenue Requirement**

In its argument-in-chief CNPI Tx provides an updated Revenue Requirement for 2015, in the amount of \$4,467,388 and for 2016, in the amount of \$4,843,623. CNPI Tx indicated that undertaking J1.3 sets out the updated revenue requirement numbers, except for the property tax error as described in J1.4. OEB staff notes that CNPI Tx did not explicitly update "operating costs", for which it is seeking OEB approval, as set out in the original application. OEB staff believes that this may be an oversight. OEB staff requests that CNPI Tx in its reply submission update, if applicable, the operating costs proposed for 2015 and 2016 so that they are aligned with the updated revenue requirement numbers. The update should provide a trail, starting with the original as filed, of the changes for each of the components-- e.g. OM&A, depreciation, income taxes -- that comprise the operating costs such that the updated operating costs align with the updated revenue requirement.

### **Capital Expenditures and Rate Base**

CNPI Tx originally requested that the OEB approve \$5,852,942 and \$740,000 in capital expenditures for the 2015 and 2016 test years respectively and a corresponding rate base of \$21,599,433 and \$24,136,519. CNPI Tx's argument- in-chief revised its revenue requirement request for 2015 and 2016 as noted in the introduction to this submission. OEB staff asks that CNPI Tx confirm in its reply argument that the associated revised rate base is the one presented in the revenue requirement work form attached to the response to undertaking J1.3, being \$20,790,755 for 2015 and \$24,211,326 for 2016. OEB staff also asks that CNPI Tx provide corresponding revised capital expenditure amounts for the test years, if applicable.

### **International Power Line**

CNPI Tx is seeking OEB approval to rebuild the International Power Line (IPL) which consists of 2 lattice towers (Queen Street Tower and Buffalo High Tower) and two

spans of wires, from Bertie Hill Tower to Queen Street Tower and from Queen Street Tower to Buffalo High Tower and covers a distance of about 1.1 km. Because of its poor condition, the IPL has been in a state of forced outage since 2013. The Queen Street and Buffalo High Towers were demolished in 2014. The existing IPL was intended as an alternative source of supply when there are outages between the Hydro One stations and CNPI Tx's Station 18. The estimated cost of the project is about \$6.9M, with \$1,790,000 spent in 2014 and the balance to be spent in 2015. CNPI Tx is proposing to close \$6.8M in expenditures to rate base in 2015.

The IPL facility, prior to its forced outage in 2013, was available to serve CNPI's customer on an as-needed basis. Using the IPL to supply CNPI's customers requires the isolation from the Ontario grid and connection into the New York transmission system. While this activity takes a few hours to coordinate, the facility nevertheless enabled quicker restoration times relative to alternatives, and thereby enhanced overall reliability and security of supply<sup>3</sup>.

Actual use of the facility has been infrequent; it was activated only once in the recent past, on a planned basis, for eight hours during a 2006 ice-storm. In May 2012, there was an incident that would have required the operation of the IPL, but it wasn't energized because the IPL itself was in a state of forced outage. As a result, CNPI Tx experienced 580 minutes (9.7 hrs.) in outage time. This outage was in excess of the 8 hour load restoration criteria established by the IESO (Ontario Resource and Transmission Assessment Criteria/August 2007). CNPI has also indicated that, without the IPL, in the near future there will be an 8 hour outage to complete work that has been put on hold on the expectation that the IPL will be rebuilt.<sup>4</sup> CNPI argues that the line is needed for the utility in order to allow system restoration within ORTAC criteria in the event of a contingency and in order to execute its vision of good utility practice.

OEB staff notes that had this proposal been for a new facility, the applicant would typically be expected to demonstrate the need for the facility, including its benefits relative to its costs, as well as to show that the IPL was the preferred option relative to alternatives. The utility would likely also have been required to establish whether any customer contribution would be called for pursuant to cost responsibility rules in the Transmission System Code.

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<sup>3</sup> The facility is characterised as a "break before make" one, in that connection with Hydro One Transmission must be physically disconnected before electricity is allowed to flow from Buffalo. The "break and make" operation takes 2-4 hours to complete.

<sup>4</sup> EB-2014-0204 transcript (oral hearing) pages 21-27.

OEB staff also notes that based on history, the frequency with which the IPL would actually be needed is low. While its absence could have a high impact on the CNPI Tx's customer and those customers of CNPI Dx, OEB staff is uncertain whether the expected frequency of outages, coupled with the transmitter's overall reliability performance, would support the need for the investment in a new facility if proposed today, if other alternatives would provide similar levels of restoration performance at lower cost, or even if the level of service was acceptable in the circumstances, and no remediation were required.

However, OEB staff acknowledges that this project is not new and accepts that CNPI Tx is merely proposing to restore an asset that has been in service for a significant period. Further, while the function of the IPL has varied over time, OEB staff is of the view that the alternate supply point has become integral to CNPI Tx's ability to maintain its historical level of service to CNPI Dx in a manner that suits the equipment it has, the skills of its staff as well as its system configuration.

In its acceptance of Hydro One's delivery point performance standards in a 2005 decision, the OEB found that it was reasonable for Hydro One to commit to maintaining historical delivery point performance standards, and endorsed the transmitter's proposal to "cover the remedial costs of restoring and sustaining the inherent reliability performance of the existing assets to what was designed originally"<sup>5</sup>. OEB staff finds considerable analogy in CNPI Tx's proposal regarding the IPL and its own customer's expectations, and accordingly accepts the appropriateness of the rebuild project. OEB staff notes that since CNPI Tx recovers its costs through Ontario uniform transmission rates ultimately paid by all Ontario electricity customers, the rate consequences of this investment will be negligible, including for CNPI distribution and its end use customers, who will benefit from it.

However, OEB staff questions the likelihood that the \$6.9M project will be completed and ready to be put into actual service, if needed, by December 31, 2015. This is a significant project that will increase CNPI's rate base<sup>6</sup> by about 40% once its full cost is embedded in rates.<sup>7</sup> The impact on the 2015 revenue requirement is about \$372,000 and \$585,000 in 2016.<sup>8</sup>

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<sup>5</sup> RP-2002-0424, Decision and Order, s 2.3.10, p 21

<sup>6</sup> Starting in 2015 there is no working capital component in CNPI Tx's rate base.

<sup>7</sup> Response to IR 2-Staff-20

<sup>8</sup> Response to IR 2-staff-20

The original expectation in the application as filed was that the ordering of materials and construction would occur between February 2015 and December 2015, a period of about 9 months.<sup>9</sup>

From	To	Action
July 2013	April 2014	Engineering, Environmental, socio-economical studies
May 2014	June 2014	NEB application filing and approval
May 2014	September 2014	Project coordination, communication plan
September 2014	November 2014	Demolition of the IPL
February 2015	October 2015	Ordering materials and construction of the new IPL

CNPI Tx indicated that it would order the materials once it had OEB approval for the project. Accordingly, to ensure completion by October 2015 it needed an OEB decision by March 1, 2015 and by May 1, 2015 to ensure completion by the end of 2015. This allows 8 months for the ordering of materials and construction. Under cross-examination CNPI Tx confirmed that the actual delivery of materials would take between 20 and 28 weeks, for an average of 24 weeks (or 4.3 months) and 2 months of construction would follow (one month of pre-delivery construction also occurs). CNPI Tx acknowledges that with a May 1, 2015 decision “.... [they] have a good chance to get it done...if you get into May, to June, to July we are going to have difficulty... this is an estimate...we cannot say for sure...because it really depends on the market condition at that time.”<sup>10</sup> CNPI Tx confirmed that prior to placing the asset into service inspection takes place during construction as well as after. To the question of a December 15, 2015 construction finish ( 7.5 months after May 1, 2015), and whether the IPL would be then operationally ready, CNPI Tx acknowledged that it would depend on the condition of the system at that time and the readiness of the US authorities to test the system so close to Christmas. CNPI Tx also noted that the question was theoretical, since inspections are done both during and at the end of construction, but concluded, if all things are coordinated with the National Grid, a matter of days would be required.

Asked whether the latter would be done at the same time as the construction, CNPI Tx replied, “We would coordinate it with construction so all parties are ready to go as the contractor is pulling away, because you wouldn't want the contractor to leave and then find a deficiency. So we would coordinate it with the contractor.”<sup>11</sup>

OEB staff submits that the likelihood that the IPL will be completed, inspected, tested and authorized for full operation by the end of 2015 is not high. There is little timetable

<sup>9</sup> Exhibit 11-1-1 page 22

<sup>10</sup> EB-2014-0204 transcript (oral hearing) page 54

<sup>11</sup> ibid

flexibility (2-3 weeks) to absorb unforeseen delays. A number of uncertainties could negatively affect the project timeline and result in a 2016 rather than 2015 in-service date, including delays to material delivery, poor coordination among parties, or lengthier than expected pre-operational approvals

In the view of OEB staff it is unreasonable to include \$372,000 in CNPI Tx's 2015 revenue requirement for a project that is unlikely to be in-service by December 31, 2015.

OEB staff submits that the IPL project should be closed to CNPI Tx's 2016 rate base; OEB staff would also expect that regular accounting conventions, such as the half year rule, would also apply.

### **Customer Delivery Point Performance Standards**

CNPI Tx has proposed Customer Delivery Point Performance Standards (CDPPS) for the OEB's approval.

Staff notes that the OEB's intent, in section 4.5.1 (d) of the TSC, is for each transmitter to develop performance standards based on its own historical performance, not the historical performance of any other transmitter. CNPI Tx's application proposes to adopt HONI's (Hydro One Networks Inc.) minimum target of 3.5 outages per year. In interrogatory #23, OEB staff requested CNPI Tx to describe its actual historical performance, which is in the range of 0.6 to 0.8 (and includes impacts from HONI's system). As such, adopting HONI's minimum target would represent a five-fold degradation in CNPI Tx's gross historical delivery point performance. Staff therefore believes that CNPI Tx's proposal is not consistent with the OEB's intent, as reflected in HONI's CDPP Standards document. That is, the CDPP Standards are intended to maintain the historical reliability performance levels at each customer delivery point (i.e., not degradation).

In its application, CNPI Tx stated, "CNPI Tx's transmission system is a radial extension of HONI's transmission system and therefore its performance is dependent upon the performance of HONI's transmission System". Staff notes that this relatively unique configuration more closely resembles delivery points that exist between a transmitter and a distributor. Staff therefore suggests that it is more appropriate to assess CNPI Tx's transmission system performance by taking CNPI Tx's historical performance and exclude upstream "Loss of Supply" as defined in the OEB's RRR reporting of

distribution system reliability. “Loss of Supply” means an interruption due to problems associated with assets owned and/or operated by another party, and/or the bulk electricity supply system impacts. Given that CNPI Tx’s transmission system is an extension of HONI’s transmission system, OEB staff suggests that CNPI Tx’s delivery point standards should be calculated and presented gross and net of HONI’s impact. Staff notes that, if this approach is approved, CNPI Tx would focus on outages solely attributable to CNPI Tx. In response to OEB staff interrogatory #23, CNPI Tx stated that any response to reliability concerns would involve consultation with HONI and using similar criteria would allow for a cooperative response. In response to OEB staff interrogatory #23, CNPI Tx stated that any response to reliability concerns would involve consultation with HONI and using similar criteria would allow for a cooperative response. Staff is of the view that the practice of cooperation should continue. Staff notes that CNPI Tx’s exhibit 2-5-1 appears to indicate that the historical outages are not attributable to HONI delivery point performance, as claimed in response to OEB staff interrogatory #23,

Should the OEB approve the refurbishment of the IPL connection, OEB staff recommends that CNPI Tx adjust its CDPPS, once this circuit is placed into service. The basis for this recommendation is founded on the fact that CNPI Tx’s most significant outage occurred while the IPL was in a forced outage, a condition that is expected to be corrected should this investment be approved and placed in-service.

CNPI Tx has only one load customer. As such, OEB staff believes Inlier standards are most applicable and they are intended to reflect actual performance. Given the above, OEB staff proposes that section of their CDPP Standards document be revised to reflect the change recommended above – ie, taking into account outages attributable to HONI. Aside from that change, OEB staff is comfortable with CNPI Tx’s proposed CDPP Standards document.

## **Operating, Maintenance and Administrative Expenses**

CNPI Tx originally proposed OM&A expenses (including property taxes) for 2015 and 2016 in the amounts of \$2,012,716 and \$2,205,066 respectively.<sup>12</sup> The last OEB approved OM&A was set in 2002 in the amount of \$1,100,790. Based on the evidence in the original application OEB staff prepared the table below. The table provides a high level summary of the reasons for the increase between 2010 actual and 2015 and 2016.

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<sup>12</sup> Exhibit 4.1.1 page 1 table 4.4.4.1



In the view of OEB staff, reference to the 2010 actual OM&A amount provides a more practical basis for comparison, given that the last OEB-approved OM&A amount was set 13 years ago.

<b>Major Cost OM&amp;A Drivers between 2010 Actual and 2015 and 2016 Test Years.</b>	
<b>2010 Actual</b>	<b>\$ 1,461,386</b>
-Shared Services	\$ 199,826
-Fortran Write-Down	\$ 122,128
-25 Hertz Removal Project	\$ 95,900
-Regulatory	\$ 36,025
-Misc.	\$ 75,351
-Operating and Maintenance	\$ 48,000
-Property Taxes	-\$ 25,900
<b>TOTAL 2015</b>	<b>\$ 2,012,716</b>
-Misc.	\$ 44,350
<b>Total 2016</b>	<b>\$ 2,057,066</b>
Sourced from E4-2-2 (Appendix 2-JB)	

Other than for the adjustments identified below, OEB staff has no further concerns with the OM&A proposed by CNPI Tx for 2015 and 2016.

#### Removal of 25 hertz Cycle Transmission Line

CNPI Tx's proposed OM&A expenditures for 2015 and 2016 each include \$150,000 for the removal of the 25 hertz cycle transmission line that was decommissioned in 2009. These expenditures are part of a removal program that started in 2010 and is detailed in the table below.<sup>13</sup>

**Table 4.3.1.2 25-cycle Transmission Line Removal Project**

<b>Year</b>		<b>Cost</b>	<b>Towers Removed</b>
2010	Actual	\$ 57,000	10
2011	Actual	\$ 52,800	10
2012	Actual	\$ 82,000	15
2013	Actual	\$ 84,300	15
2014	Forecast	\$ 99,000	15
2015	Test Year	\$ 150,000	30
2016	Test Year	\$ 150,000	30
2017	Forecast	\$ 150,000	30
2018	Forecast	\$ 150,000	30
<b>Total</b>		<b>\$ 975,100</b>	<b>185</b>

<sup>13</sup> Exhibit 4-3-1 page 2

From the table, it is apparent that the pace of the program has recently accelerated since its inception in 2010. During 2013-2014 the number of towers removed increased by 50% and for the 2015-2016 CNPI Tx is planning to increase the number of towers to be removed annually by a further 100%.

CNPI Tx justifies the acceleration in pace of tower replacement in the test period on the basis of public safety concerns and an increase in public complaints. Although the removal program started in 2010, CNPI Tx indicated that it was only in 2012 that they realized the poor condition of towers in residential areas and in 2013 they noticed rusting, and birds nesting that would require additional removal costs because of environmental protection requirements if left unabated.<sup>14</sup> CNPI Tx also indicated that the acceleration plan had to also consider "...that [it] has to balance with budget...within financial means..."<sup>15</sup> CNPI Tx in acknowledging that it has over-earned between 16% and 21% over the past 4 or five years, stated that if public safety were an issue monies would not be held back.<sup>16</sup> As to why CNPI Tx did not accelerate to 30 towers in 2013 and 2014, CNPI Tx explained that "there is a lead time... to make sure it fits in our resources and our own internal budgeting year...2014 was already committed [and] already approved with in our own internal management ...so 2015 was the first available..."<sup>17</sup> CNPI Tx also noted that that they need 2013-2014 to transition to the higher rate of tower removals and that the restriction in 2013 and 2014 was a technical and not a monetary one.<sup>18</sup>

OEB staff questions the urgency that requires a doubling of the tower removal, from 15 to 30, in each of 2015 and 2016. The 25 Hertz transmission was decommissioned in 2010 and it took about 2 years for CNPI Tx to notice its poor condition and the fact that birds were nesting in the structures. OEB staff submits that in its view CNPI appears to date to have displayed little sense of urgency, since although there were more than enough funds available during 2012, 2013 and 2014 the pace of acceleration was constrained by internal planning and budgeting practicalities. OEB staff would expect a company such as CNPI Tx would be able to speed up its internal processes for what it considers a priority.

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<sup>14</sup> EB-2014-0204 transcript (oral hearing) pages 89-91

<sup>15</sup> EB-2014-0204 transcript (technical conference) page 45

<sup>16</sup> EB-2014-0204 transcript (oral hearing) pages 94-95

<sup>17</sup> *ibid.* pages 95-96

<sup>18</sup> *Ibid.* page 96

OEB staff submits that the OM&A expenses proposed for 2015 and 2016 be each reduced by \$58,000 <sup>19</sup> to reflect the actual recent pace of the program.

### One-time Regulatory Expenses

2015 and 2016 Test Year OM&A expenses each include \$36,025 for the forecasted costs of the instant proceeding amortized over 5 years.

Table: 4.7.1.1 One Time Cost Summary

One-Time Cost Summary	
Intervenor costs	49,245
Legal Costs	90,000
Consultants' Costs	40,880
	<u>180,125</u>
Cost per year over 5 years	36,025

OEB staff notes that there are no active intervenors in this proceeding and the level of activity has been comparatively low: the technical conference took one day, there was no settlement conference (and therefore also no time invested in drafting a settlement proposal); and the oral hearing lasted just one day. OEB staff submits that the \$180,125 should be reduced by \$49,245 in intervenor costs and \$30,000 in legal costs and \$5,000 in consultant costs. On this basis, the annual amount in 2015 and 2016 should be reduced by \$16,849.

### Salaries and Wages

CNPI Tx's proposed OM&A contains a provision for salary and wage increases of 3% (June 2014) and 3.1% (June 2015) as contracted for unionized staff and 3% for non-unionized employees in each of 2015 and 2016. In response to interrogatory 4-staff-37, CNPI Tx indicated that the 2015 and 2016 OM&A would be reduced by \$10,000 and \$20,000 respectively, if increases were more in keeping the forecasted rate of inflation, which CNPI Tx took to be 2.0%.<sup>20</sup>

OEB staff submits that the provision for salaries and wages increases should be limited to the forecasted rate of inflation, and should not be considered as an automatic add-on. CNPI Tx did not identify any specific actions it has taken to allow it to operate within the rate of inflation.

<sup>19</sup>  $\$150,000 - [(\$84,300 + \$99,000)/2]$

<sup>20</sup> Interrogatory response 4-Staff-37

## Project Fortran

Project Fortran is addressed later in submission.

### **Capital Structure and Cost of Capital**

The return on equity, the rate for the affiliated promissory note and short term debt rate reflected in the application as filed are those approved by the OEB in its letter on capital cost parameters dated November 25, 2013. CNPI Tx indicated in its application that it would update the aforementioned rates in accordance with the OEB's cost of capital parameters current at the time of the OEB's decision. OEB staff asks that CNPI Tx in its reply argument identify at which stage of the process it proposes to file with the OEB updated numbers which reflect the capital cost parameters issued by the OEB on November 20, 2014.

### **Regulatory Accounting**

#### Effective Date of Changes in Accounting Policy

OEB staff notes that for the most part, the OEB has historically issued little guidance, accounting or otherwise, that was specific to transmitters. The OEB has generally applied its instructions to distributors and transmitters uniformly. For example, until 2014, filing requirements for cost of service applied equally to transmitters and distributors.

The specificity of OEB instructions is intrinsic to the issue of CNPI Tx's adoption of changes to the useful lives of its assets. In a July 2012 letter, the OEB permitted electricity distributors to implement regulatory accounting changes for depreciation expense and capitalization policies effective January 1, 2012 and made them mandatory by January 1, 2013. The letter was not specifically addressed to transmitters.

CNPI Tx indicated in this application that it changed its accounting policies effective January 1, 2015. Useful lives of its assets were changed to be consistent with the Asset Depreciation Study for the Ontario Energy Board, July 8, 2010. No changes to its capitalization policy were required as its capitalization policy was already consistent with the capitalization policy clarified by the OEB in its letter regarding Accounting for Overhead Costs Associated with Capital Work, February 24, 2010. In the technical conference, CNPI Tx stated that it changed the useful lives of its assets effective January 1, 2015 as that is the effective date for the requested rates in this rate

application and it is seeking the OEB's approval to change useful lives in this rate application.

If CNPI Tx had implemented the changes in 2013, CNPI Tx estimated that its property, plant and equipment as at December 31, 2014 would be about \$465,000 greater, equating to \$19.5 million. This would also create a credit balance of about \$465,000 before the rate of return in Account 1576 Accounting Changes Under CGAAP.<sup>21</sup> While a current credit balance would be available to be disposed, OEB staff notes that the over the remaining updated lives of the facilities, this credit will be offset by higher rate base in future years.

CNPI Tx indicated that it did not make the changes to its accounting policies in 2013 in accordance with the OEB letter dated July 17, 2012, as the letter was directed to electricity distributors and not transmitters. CNPI Tx also stated that it did not believe Account 1576 applied to transmitters.

CNPI Tx has adopted Accounting Standards for Private Enterprises (ASPE). The below submission makes references to IFRS, but OEB staff is of the view that the same arguments hold for CNPI Tx's transition to ASPE as the intent of the policy is to capture the impacts of a transition in accounting standards.

OEB staff acknowledges the absence of guidance to transmitters specifically in these OEB communications; however, OEB staff notes that CNPI Tx made changes to its accounting policies nevertheless, except with an effective date of January 1, 2015. CNPI Tx stated that it changed the useful lives of its assets effective January 1, 2015 as this is the effective date for the requested rates in this rate application and it is seeking the OEB's approval to change useful lives in this application.

In addition, OEB staff notes that one of the reasons the OEB mandated the accounting policy changes was so that the changes would be applied uniformly. The OEB's letter dated July 17, 2012 states:

A key benefit that was expected to be derived from the OEB's established accounting policies under the IFRS framework ("modified IFRS") was that the changes to the depreciation expense and capitalization policies would be applied uniformly and in the same timeline by all distributors (with a few

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<sup>21</sup> EB-2014-0204 technical conference undertaking JT1.1

exceptions, for example, distributors adopting US GAAP).

OEB staff notes that in its rate application for 2013 and 2014 rates (EB-2012-0300), Great Lakes Power Transmission LP indicated that it adopted IFRS effective January 1, 2013. It used Account 1575 to record the differences in depreciation expense and net book value of assets approved for retirement recovery in its transition to IFRS. The OEB approved the settlement agreement, which disposed of Account 1575. In that case, the balance was a debit (i.e. collectible from ratepayers).

Hydro One Transmission has been reviewing and updating its capitalization and depreciation policies throughout various past rate applications. It began reviewing its overhead capitalization rate on a quarterly basis starting in 2007.<sup>22</sup> Hydro One Transmission was also directed to conduct a critical review of its capitalization policies; the results were reflected in its rate application for 2013 and 2014 rates. Hydro One Transmission also conducted and updated depreciation studies to support its depreciation expense for its rate applications pertaining to 2009 and 2010, 2013 and 2014, and 2015 and 2016<sup>23</sup>. CNPI Tx has not been updating its useful lives on a regular basis.

Given that the two transmitters noted above have already implemented its accounting policy changes, OEB staff submits that the OEB may wish to consider the applicability of the January 1, 2013 effective date to CNPI Tx.

OEB staff notes that as CNPI Tx's effective date of the accounting policy changes coincides with the test period beginning January 1, 2015, there would be no amounts to be recorded in Account 1576. As previously mentioned, if the accounting policy changes were made January 1, 2013, a credit of about \$465,000 would be recorded in Account 1576. OEB staff also notes that CNPI Tx adopted ASPE effective January 1, 2011 and not January 1, 2015.

CNPI Tx's capital assets contain a small portion that is allocated from CNPI Distribution. CNPI Distribution made accounting policy changes effective January 1, 2013. As such, it is noted that there is inconsistency in CNPI Tx's capital assets in that they contain transmission assets that have useful lives changes made effective January 1, 2015 and allocated distribution assets that have useful lives changes made effective January 1,

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<sup>22</sup> EB-2014-0140 Exhibit C1, Tab 7, Schedule 1

<sup>23</sup> EB-2014-0140 Exhibit C1, Tab 7, Schedule 1, EB-2012-0031 Exhibit C1, Tab 8, Schedule 1

2013.

In addition, the Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment (EB-2008-0408), June 13, 2011, which is the basis for the development and establishment of Account 1575 IFRS-CGAAP Transitional PP&E Amounts and Account 1576, states:

This Addendum, consistent with the 2009 Report, focuses on electricity distributors and rate-regulated natural gas utilities. However, the Board will have regard to the policy and rationale for the policy in this Addendum when considering similar issues for other regulated entities.

Finally, OEB staff observes that CNPI Tx refers to and therefore, relies on various OEB guidance for IFRS for electricity distributors<sup>24</sup> to justify its capitalization and depreciation policy proposals for the subject application.<sup>25</sup> As such, OEB staff submits that the OEB is not limited to applying the guidance that it has developed for electricity distributors.

Account 1592 PILs and Tax Variances for 2006 and Subsequent Years, Sub-account HST / OVAT Input Tax Credits

Account 1592 PILs and Tax Variances for 2006 and Subsequent Years, Sub-account HST / OVAT Input Tax Credits (ITCs) was established by the OEB to record the incremental ITC they receive on distribution revenue requirement items that were previously subject to PST and became subject to HST. CNPI Tx is of the view that the direction from the OEB for the sub-account of Account 1592 applies to electricity distributors and not transmitters. In an undertaking to the oral hearing, CNPI Tx indicated that the total savings that would have been recorded in the sub-account is \$16,000.

OEB staff notes that this amount is immaterial and takes no issue with it for this reason. However, staff submits that the OEB's policy on transitional accounting matters and tax law changes has been clear: to keep customers whole. Utilities should not be enriched by changes in tax rates or rules. The lack of specific identification or reference to transmitters in many OEB policies is not new. While guidance from the OEB could well have been clearer, OEB staff would expect that a regulated entity acting in the interests

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<sup>24</sup> Board's February 24, 2010 letter regarding *Accounting for Overhead Costs Associated with Capital Work* and *Asset Depreciation Study for the Ontario Energy Board*, July 8, 2010

<sup>25</sup> Exhibit 1-1-11 page 1

of its customers and aware of broader policy precedent would take steps to adhere to the OEB's broad principles even if discrete circumstances do not remove all ambiguity about what is expected of them.

#### Project Fortran

CNPI is seeking to recover \$1,221,281 in relation to pre-development costs related to Project Fortran. CNPI Tx proposes to recover this amount over a 10 year period. Project Fortran was a proposal by CNPI Tx to build a synchronous interconnection between Fort Erie and the United States. In 2009 CNPI Tx filed a leave to construct application with the OEB for the project. The estimated cost of Project Fortran was \$33.2M.

The OEB denied the application. The OEB held that the project was not justified on the basis of improved reliability, and that there was not a strong economic case for the intertie.

Although the OEB denied the application, CNPI Tx had already incurred approximately \$1.5M in costs related to certain pre-construction activities, such as feasibility and impact studies. CNPI Tx had booked these costs in its construction work in progress account. After the leave to construct application was denied, CNPI Tx filed an application with the OEB seeking permission to create a deferral account into which the \$1.5M could be recorded for future disposition (EB-2010-0159).

The OEB denied this request. The OEB noted that CNPI Tx had not re-based since 2001, and stated: "[i]f CNPI Tx foresaw expenses that it could not afford within its current revenue envelope it should have applied to the Board prior to incurring the expense to have the merits of its new revenue requirement tested."

OEB staff submits that CNPI Tx's request to recover costs related to Project Fortran should be denied for two reasons: 1) it would amount to retroactive rate making, and 2) the OEB has already denied this request.

It is a well-known principle of rate making law that the OEB is generally not permitted to set rates on a retroactive basis. The OEB cannot adjust rates on a going forward basis to account for things that occurred in the past. There are a number of exceptions to this rule, the most important of which is deferral or variance accounts. However, in order to function, a deferral (or variance) account should be established before the expense is



incurred.

There appears to be little question that the amounts CNPI Tx is seeking to recover are retroactive. They were incurred in the period leading up to the leave to construct application in 2009. Although CNPI Tx booked these amounts in their own construction work in progress account, this is not an OEB-approved deferral or variance account. To allow CNPI Tx to recover these amounts starting in 2015 would be a clear case of retroactive ratemaking.

In addition, the OEB has already considered this issue and denied CNPI Tx's request. Although CNPI Tx was seeking a deferral account in EB-2010-0159 as opposed to an immediate recovery of the Project Fortran costs in rates, in effect these amount to the same thing. CNPI Tx requested a deferral account to allow it to recover the costs from ratepayers at a later date. The OEB considered the issue and denied the request. CNPI Tx did not file a motion to review or an appeal of this decision. The OEB's decision is therefore final and CNPI Tx should not be permitted to make what is essentially the same request again.

CNPI Tx argues that the costs were prudently incurred, and therefore should be approved. OEB staff disagrees. Whether or not the costs were prudent, they were out of period and have already been considered and denied by the OEB. For these reasons, OEB staff submits that CNPI Tx's request to recover costs related to Project Fortran should be denied.

#### Calculation of Uniform Transmission Rates

CNPI Tx requested that the update the Uniform Transmission Rates (UTR) to allow recovery of the proposed revenue requirements for 2015 and 2016, effective January 1 of each of these Test Years. On December 18, 2014, the OEB declared the CNPI Tx's existing revenue requirement interim effective January 1, 2015.<sup>26</sup>

In the event that the OEB approves January 1, 2015 as the effective date, OEB staff submits that a deferral account be established to record the foregone revenue for future disposition. OEB staff requests that CNPI Tx include a draft accounting order for such an account in its reply submission.

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<sup>26</sup> EB-2014-0204 Order for Rates

*All of which is respectfully submitted.*