

# AIRD & BERLIS LLP

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April 7, 2015

## VIA COURIER, EMAIL AND RESS

Ms. Kirsten Walli  
Board Secretary  
Ontario Energy Board  
2300 Yonge Street, 27<sup>th</sup> Floor  
Toronto, ON M4P 1E4

Dear Ms. Walli:

**Re: Niagara Peninsula Energy Inc. 2015 Cost of Service Rate Application  
Board File No. EB-2014-0096**

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We are counsel to the Applicant, Niagara Peninsula Energy Inc. ("NPEI"), in the above noted proceeding.

Please find attached the Reply Submissions of NPEI.

If there are any questions, please contact the undersigned.

Yours very truly,

**AIRD & BERLIS LLP**



Scott Stoll

SAS/bm

cc: Case Manager, Christie Clark (*via email*)  
Board Counsel, Maureen Helt (*via email*)  
Intervenors (*via email*)

Encl.

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**EB-2014-0096**

**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

**REPLY SUBMISSIONS OF  
NIAGARA PENINSULA ENERGY INC.  
("NPEI")**

1. The Board should grant approval of the 13% working capital allowance requested by NPEI and should set a fixed-variable rate for the residential customer class with guidance on the future transition of the fixed-variable split. NPEI is replying to the submissions of the Energy Probe Research Foundation ("**Energy Probe**"), the School Energy Coalition ("**SEC**"), Vulnerable Energy Consumers Coalition ("**VECC**") and Board Staff on the two issues that were not settled in this proceeding: (a) the rate design for fixed-variable split; and (b) the working capital allowance percentage.
2. NPEI used the Board approved process in applying for a 13% working capital allowance and Board Staff has supported the request for the 13% working capital allowance. The Intervenor has failed to provide any evidence that would warrant deviating from the well-established Board practice of accepting the 13% working capital allowance in the absence of a lead-lag study. SEC has explicitly acknowledged this evidentiary shortcoming by suggesting the alternative of re-opening the evidentiary phase of the proceeding and ordering a lead-lag study – a time consuming and costly exercise at this time.
3. As a result of the response to Undertaking J1.1, NPEI has amended its request and no longer is seeking to adjust the fixed-variable split from the current 58:42 split to a ratio of 65:35.

**Fixed-Variable Split**

4. NPEI originally was seeking to increase the fixed portion of the residential rate class from the current 58% to 65%. This would have returned the fixed portion to the historical

fixed portion of the rate used by Niagara Falls Hydro Corporation ("**NF Hydro**"), one of the predecessors to NPEI. NPEI is no longer seeking such relief.

5. In response to Undertaking J1.1, NPEI provided the consumption level, 711kWh, at which customers would be indifferent between the existing fixed-variable split and the NPEI proposed 65:35 fixed-variable split.
6. While completing Undertaking J1.1, NPEI voluntarily went further than the specific undertaking to determine the number of customers above and below that crossover point. In doing so, NPEI acknowledged that more customers would benefit from maintaining the current fixed-variable split as compared moving to a 65:35 fixed-variable split.
7. In oral submissions, NPEI indicated three principles behind its proposal to increase the fixed component of the residential bill. These principles included: (a) consistency with NPEI's understanding of Board policy; (b) a return to the historic fixed-variable split of the former NF Hydro; and (c) the understanding that the proposal would benefit a greater number of the customers in the rate class.
8. However, given the new evidence from the response to Undertaking J1.1, NPEI's request was no longer consistent with the third principle.
9. As a result and despite the other two principles, NPEI indicated it was no longer requesting the 65:35 split as part of this Application due to the number of customers that would benefit from retaining the current fixed-variable split. NPEI still strongly supports the other two principles but understands the customer impact in this particular circumstance.
10. On April 2, 2015, the Board released the Board Policy, A New Distribution Rate Design for Residential Electricity Customers in which the Board stated "*electricity distributors will structure residential rates so that all the costs for distribution service are collected through a fixed monthly charge*" (the "**Policy**"). Previous to the publication of the Policy, the Board had provided commentary on this subject, but the Policy represents the first public commitment to the proposed changes to the fixed-variable split.
11. The newly issued Board Policy provides a direction for distributors and the setting of residential rates over the next few years. As such, NPEI's prior request was consistent with the new policy.
12. Therefore, NPEI requests the Board maintain the current fixed-variable split of 58-42 and would request direction from the Board regarding the transition contemplated by the Policy.

#### **Working Capital Allowance Percentage**

13. NPEI applied for a 13% allowance using the default amount provided by the Board in its letter dated April 12, 2012 which explained changes to the Board's 2013 Filing

Guidelines. In that letter, distributors were given 2 options – (1) the filing of a lead-lag study; or (2) the use of the 13% default value.

14. Intervenors' suggestions of a working capital percentage other than 13% is inconsistent with Board policy; not based on evidence sufficient to deviate from Board policy; relies upon changes that occurred prior to the previous rate case, EB-2010-0138; and fails to recognize any changes that would tend to increase the need for working capital.
15. The Board has consistently held that absent a lead-lag study for the utility in question, the Board would not deviate from the 13% working capital allowance. NPEI was not ordered to conduct a lead-lag study in its last cost of service proceeding. NPEI, as was its right, chose to use the default value of 13% provided for in the guideline. Board Staff noted that NPEI has followed the Board's policies for WCA and supported NPEI's approach.
16. NPEI, as part of the Settlement Agreement, agreed to conduct a lead-lag study prior to its next rebasing. It is NPEI's submission that SEC's request to re-open the evidence this hearing to have a lead-lag study conducted is not timely and is a collateral attack on the Settlement Agreement to which SEC is a party.

Background

17. NPEI is the result of the merger of the former NF Hydro and Peninsula West Utilities Limited ("PWU") which took effect January 1, 2008. PWU billed its residential customers monthly and NF Hydro billed its residential customers bi-monthly at the time of the merger.
18. Effective May 1, 2010, NPEI switched its residential customers in the former NF Hydro service territory to monthly billing.<sup>1</sup> In preparation for that switch, Ms. Wilson provided the Board of Directors with a cost-benefit analysis of the impact of the proposed switch to monthly billing.<sup>2</sup>
19. Ms. Wilson testified that the memorandum she wrote to the Board of Directors that Intervenors are attempting to rely upon as justification for their request was a cost-benefit analysis – not a cash flow analysis.<sup>3</sup>
20. On May 30, 2011, a full 13 months after monthly billing was implemented, the Board issued its decision in EB-2010-0138. As such, the switch to monthly billing should be irrelevant to the present proceeding.
21. In May of 2014, NPEI discontinued billing for water for the City of Niagara Falls. This resulted in a final payment of approximately \$8.6 million from NPEI to the City of Niagara Falls.<sup>4</sup>

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<sup>1</sup> Tr. Vol. 1, March 17, 2015, Page 22, lines 6 to 8.

<sup>2</sup> Exhibit K1.3, Energy Probe Compendium, pages 15 and 16. Note the date on the memorandum is incorrect. The precise date is not known but it was written prior to May 1, 2010.

<sup>3</sup> Tr. Vol. 1, March 17, page 67, lines 19 to 28.

22. The effects of the removal of the water billing were incorporated into the Operations, Maintenance and Administration spending for the 2015 Test Year in the proposed Settlement Agreement which was put forward by all of the Intervenor along with NPEI.
23. Since EB-2010-0138, NPEI has taken on \$30 million in new debt to continue to operate its business.<sup>5</sup> In addition, NPEI increased its operating line of credit by \$2 million because of the increased cost of power. NPEI noted that it had gone into overdraft in September 2014.<sup>6</sup>

Board Policy and Desirability for Consistency

24. NPEI is of the view that any working capital allowance other than 13% represents a significant departure from the well-established Board practice. While the Board is not strictly bound by previous decisions, there is considerable precedential value from the decisions and the goals of consistency and predictability in decision making is fostered through adherence to the Board's guideline and prior decisions. Only in the clearest of cases, with the presence of compelling evidence, should the Board depart from its stated guidelines.
25. On April 17, 2012, the Board issued a letter to all licensed electricity distributors entitled "update to Chapter 2 of the filing requirements for transmission and distribution applications allowance for working capital", which update the options for the calculation of the working capital allowance for the 2013 rate year. Prior to the letter, the Board's filing requirements for cost-of-service distribution rate applications provided for a 15 percent rate to be used for the calculation of the working capital allowance. However, in the April 12, 2012 letter the OEB stated:

The Board has reviewed the approaches to the calculation of WCA and will not require distributors to file lead/lag studies for 2013 rates, unless they are required to do so as a result of previous Board decision.
26. The Board determined that the default value going forward would be 13% of the sum of cost of power and controllable expenses and that this rate would be applicable to the 2013 rate applications and beyond. That policy has not changed and that is what NPEI included in its Application.
27. This requirement is reflected in section 2.5.1.3 of the filing requirements for electricity distribution rate applications, which describes the Board's expectation with respect to the working capital allowance and allows for the default 13% approach in the absence of previous Board direction to undertake a lead/lag study.
28. NPEI would note that the dominant practice amongst distributors is to use the 13% default WCA. Ten of the eleven 2014 cost-of-service filers used the 13% WCA in their

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<sup>4</sup> Tr. Vol. 1, March 17, 2015, page 64, lines 12 to 15.

<sup>5</sup> Tr. Vol. 1, March 17, 2015, page 65, lines 14 to 18.

<sup>6</sup> Tr. Vol. 1, March 17, 2015, page 67, lines 2 to 8.

applications. Only Veridian, which had previously agreed in 2012 to file a lead/lag study, did not use the 13% default value. The 13% WCA has been accepted by the Board in a number of decisions, such as Burlington Hydro, Oakville Hydro, Kitchener Wilmot Hydro Inc., Cooperative Hydro Embrun, Fort Frances Power Corporation, and Hydro Hawkesbury.<sup>7</sup>

29. NPEI understands the Board accepted the use of 13% for WCA for at least 3 of the utilities, Co-operative Hydro Embrun, Hydro Hawkesbury and Fort Frances, which are monthly billing utilities. Of note, the Board stated:

It does 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.<sup>8</sup>

30. NPEI would also commend the panel to the recent decision in EB-2013-0147/EB-2014-0155 where the Board stated:

The Board 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 utility-specific WCA value for each case from other lead/lag studies which may not reflect the unique circumstance of such utility.<sup>9</sup>

31. The Board went on to state:

The Board finds that there is no compelling evidence in this case to suggest that a WCA value other than the default 13% was more appropriate and, therefore, confirms its earlier finding that KWHI proposed 13% is acceptable.<sup>10</sup>

32. During cross-examination, Ms. Wilson confirmed NPEI's position that it was not appropriate to use the results of a lead lag study from a different utility for NPEI.

MR. AIKEN: Okay. Would you agree that it is not appropriate to use a default value for the working capital allowance that is at a higher level than those resulting from lead lag studies?

MS. WILSON: I don't agree with that.

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<sup>7</sup> Burlington Hydro [EB-2013-0115], Oakville Hydro [EB-2013-0159], Kitchener Wilmot Hydro Inc. [EB-2013-0147/EB-2014-0155], Cooperative Hydro Embrun Inc. [EB-2013-0122], Fort Frances Power Corporation [EB-2013-0130], and Hydro Hawkesbury [EB-2013-0139].

<sup>8</sup> EB-2013-0139, Decision and Order dated January 30, 2014, Ontario Energy Board, page 10. See, also, EB-2013-0122, Decision and Order, Ontario Energy Board dated December 23, 2013, at page 4.

<sup>9</sup> EB-2013-0147/EB-2014-0155, Decision, OEB, page 4.

<sup>10</sup> EB-2013-0147/EB-2014-0155, Decision, OEB, page 4.

MR. AIKEN: Can you explain why?

MS. WILSON: I think you have to look at the individual circumstances for each utility if they are directed to do a lead lag study, to see if that utility is coming close to what the Ontario Energy Board has issued for a guideline.

So without us having to do -- having done a lead lag study, I couldn't tell you if it was appropriate for our utility or not. I am not even sure 13 percent is enough for our utility.<sup>11</sup>

33. Not only was this position not seriously challenged, but Ms. Wilson noted that without having done a lead lag study no conclusions could be drawn from one utility to another.
34. In fact, Energy Probe clearly confirmed that a utility need for working capital was utility specific by providing reference to a few large utilities that each had unique working capital requirements.<sup>12</sup> In reviewing the information it is clear there is a wide range of working capital percentages even despite the fact that certain these utilities billed with the same frequencies. Therefore, the logical conclusion is other factors must impact the results of the lead-lag study.
35. While, NPEI acknowledged that all other things being equal a monthly billing utility would have less demand for working capital than the same utility if it billed every two months, the Board has consistently approved the 13% working capital allowance for both monthly and bi-monthly billing utilities. As noted by NPEI, monthly billing was just one of many factors that would impact a lead/lag study.
36. As such, in the present case there is no lead-lag study to deviate from the Board's guideline and no reason to apply a lead-lag study from a second utility. The 13% working capital allowance is the best decision.

Specific Issues Raised –Need for Increased Working Capital Allowance

37. While NPEI submits there is adequate support for its position in respect of Board policy, NPEI feels it appropriate to respond to certain additional points included in the record. However, the Intervenor have taken a selective approach – ignoring current facts and any item which would tend to increase the amount of working capital required.
38. NPEI has significant concerns about the reliance that should be placed upon evidence that pertains to a change that occurred 5 years ago. In respect of the memorandum, Ms. Wilson testified that it was not prepared as a working cash analysis but rather as a cost benefit analysis. It is improper to give that memorandum any significant evidentiary value in determining the requirements for working capital in 2015.

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<sup>11</sup> Tr. Vol. 1, March 17, 2015, page 36, line 20 to page 37, line 6.

<sup>12</sup> Exhibit K1.3, Energy Probe Compendium, page 17.

39. As noted, the memorandum was written and the billing change occurred more than 1 year before the Board's decision in EB-2010-0138. As Ms. Wilson, confirmed monthly billing was in the 2011 rates.<sup>13</sup> It seems that Intervenor's are displeased with the result from that case and are attempting to make up for it in this case.
40. Further, Ms. Wilson's testimony is clear that any working cash benefit from switching to monthly billing was more than eaten up by the increase in the cost of power<sup>14</sup> which has exceeded \$2.95 million per month on average. Further, it is clear that the factors, such as postage, included in that memorandum have changed and would lead to a different calculation.
41. Table 1 below highlights the fact that the cost of power per dollar of working capital allowance has increased by 17% - meaning NPEI must be much more efficient in using its cash.

Item (A)	EB-2010-0138 (B)	EB-2014-0096 (C)	Variance (D) = (C)-(B)	Percent (E)= (D)/(B) x 100
Cost of Power	\$108,840,807	\$144,149,669	\$35,308,862	32%
WCA %	15%	13%		
WCA	\$18,437,623	\$20,874,706	\$2,437,083	13%
Rate Base	\$119,567,690	\$160,574,664	\$41,006,974	34%
Cost of Power/\$WCA	5.90	6.91	1.01	17%
<b>Other Factors:</b>				
Account 1576		\$3,455,334	(\$3,455,334)	

42. Since EB-2010-0138, the cost of power has risen by approximately 32% which means NPEI's ratio of revenue to working capital has increased significantly from 5.90 to 6.91. This issue has been exacerbated by the 34% in rate base. This would confirm NPEI has continued to improve the efficiency of the use of every dollar of working capital allowance.
43. During the course of the IRM it is likely the cost of power will continue to rise at a rate that exceeds the formulaic increase that NPEI will receive for distribution rates. Further, given the capital plans in place for NPEI, rate base will also increase in a similar pattern. These changes will require additional working capital in the future.
44. NPEI has inferred that Intervenor's believe the Board policy provides a surplus or windfall for utilities. However, Ms. Wilson's testimony, see below, was clear that there has been no surplus in the past and the reduction from 15% to 13% in working capital allowance will further increase the pressure of managing the working cash.

<sup>13</sup> Tr. Vol. 1, March 17, 2015, page 60 line 21 to page 61, line 4.

<sup>14</sup> Tr. Vol. 1, March 17, 2015, page 45, lines 9 to page 46, line 6.



MR. SHEPHERD: But now, when the water billing is gone, you want the Board to say, Oh, but now you don't have that cash any more, the cash you never gave the ratepayers credit for earlier. Now you want to say, Oh, the ratepayers have to pay that cost, right?

MS. WILSON: I am saying I never had enough money in the last three years, that I've had to go take three \$10 million loans, and that was based on a calculation of 15 percent working capital allowance, which is now being reduced to 13 percent and the loss of water.<sup>15</sup>

45. Intervenor has failed to realize or chose to ignore other items which could create a need for increased amounts of working capital, that must be considered for NPEI, including:
  - (a) The new rate rider;
  - (b) The additional loans;
  - (c) Loans coming due; and
  - (d) The impact of losing the waterbilling.
46. NPEI is not suggesting the above list is comprehensive but rather is demonstrative of the inadequacy of the Intervenor's analysis.
47. As a result of accounting changes, NPEI is returning \$3,455,334, to ratepayers each year for the next two years. There is no revenue or cash inflow in respect of these monies – but there is an obligation to pay customers. Ms Wilson, in responding to Member Duff, confirmed NPEI's ability to meet this obligation was a result of the timing of other changes and but for those changes, a different application may have resulted.<sup>16</sup>
48. NPEI noted that it has taken on \$30million in debt since EB-2010-0138. It was clear these monies were needed to operate the business. Energy Probe's submission that the additional loans are compensated for through debt ignores the deemed capital structure of a utility and the way rate base is determined. Further, it ignores the realities of operating a business.
49. NPEI would note that the definition of working capital allowance used by intervenors, current assets minus current liabilities<sup>17</sup>, has certain limitations.
50. For example, there may be a cyclical nature within a month or within a year for which working capital requirements are needed. The working capital calculation may be quite different if the date of the calculation was completed immediately following receipt of the IESO invoice as opposed to the end of the month.

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<sup>15</sup> Tr. Vol.1, March 17, 2015, page 65, lines 9 to 18.

<sup>16</sup> Tr. Vol. 1, March 17, 2015, page 17, line 19 to page 18, line 15.

<sup>17</sup> VECC Submissions, page 4.

51. Further, the transition of assets and liabilities to current assets and current liabilities should also be considered. A review of the evidence indicates that NPEI has a loan coming due in 2015 and so that loan would be considered a current liability whereas in prior years it would not be considered a current liability. NPEI would note that it has several loans coming due during the IRM period.<sup>18</sup> These loans will impact the working capital calculation and have not been considered by the Intervenor.
52. NPEI would submit that working capital is to provide sufficient working capital resources for the period during which demand is greatest which may differ significantly from the date used for a snapshot of the utility's audited financial statements.
53. Therefore, NPEI would caution against the use of balance sheet calculations – especially from prior years for calculating current and future working capital requirements.
54. NPEI disagrees with VECC's statement that the obligation is to operate the utility at the least cost to ratepayers for essential short term requirements. With respect, the law has consistently held there is a balancing between lower costs and sufficient revenue for a long term healthy utility. The OEB Act explicitly incorporates this objective for the Board to consider in section 1, paragraph 2.
1. (1) The Board, in carrying out its responsibilities under this or any other Act in relation to electricity, shall be guided by the following objectives:.....
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.
55. The objective includes efficiency, and maintenance of a financially viable electricity industry. Had the legislature wished to provide a least cost objective, it would have clearly done so.
56. Finally, NPEI would like to address the issue of water billing. Ratepayers had benefitted from NPEI providing water billing services for years. NPEI no longer performs that activity.
57. Ms. Wilson acknowledged that the fact it no longer does water billing for the City of Niagara Falls created a need to take an additional loan.

MS. WILSON: I had to pay out \$8.6 million on the finalization of water. I took a \$10 million loan in November of 2014. We actually went into overdraft in September of 2014, which we were in the current process of getting all of the Board approvals, shareholders' approval, and the RFP, which was done in October, for us to take on the money in November.

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<sup>18</sup> EB-2014-0096, Exhibit 5, Tab 1, Schedule 1, page 3.

I also went through and increased our operating line of credit, because the power bills that we are currently seeing on a monthly basis are -- were higher than the \$8 million operating line of credit that I currently had in place, so I went through the process of updating that to \$10 million. No lead lag study was going to tell me to do that. You just do it.<sup>19</sup>

- 58. What is clear from this statement is NPEI has not had any surplus working capital under a 15% working capital allowance and it will definitely not have a surplus based on a 13% working capital allowance.
- 59. The factors discussed above create a need for a greater amount of working capital and more than offset any perceived reduction from a switch of a segment of the customer base to monthly billing. Therefore, NPEI has clearly demonstrated through these limited examples the inadequacy of the Intervenor's evidence to suggest a deviation from the 13% working capital allowance.

#### **Proposal to Require a Lead-Lag Study**

- 60. NPEI strenuously opposes SEC's suggestion that the Board should order the re-opening of the evidentiary phase of this hearing and the completion of a lead-lag study. The Board should reject the SEC request because of the additional costs and the timing of the request are effectively a collateral attack on the Settlement Agreement. Such a suggestion would force NPEI to incur significant costs for which it has no express right of recovery and would delay the conclusion of this proceeding by several months.
- 61. SEC's request highlights the fact that SEC does not believe it has sufficient evidence on the record to depart from the 13% working capital allowance. If SEC truly believed sufficient evidence existed, there would be no need for such a request. However, the request recognizes the reality that there is no basis upon which the Board should depart from its current policy.
- 62. If NPEI were ordered to complete a lead-lag study, it would need to conduct a request for proposals to engage a properly qualified consultant to perform the work. NPEI staff would not only be engaged to design and review the request for proposals but would be required to work with the consultant to provide the necessary information to complete a proper lead-lag study. The consultant would have to complete the work and write the report prior to NPEI reviewing it and submitting it as evidence. Once filed, the evidence would be subject to intervenor and Board Staff scrutiny and argument. It is likely NPEI would be responsible for Intervenor and additional Board costs. It is likely this process would take several months and considerable resources.
- 63. As the Board is aware, the parties filed a partial proposed Settlement Agreement in this proceeding. The Board panel confirmed its acceptance of the Proposed Settlement Agreement which includes acceptance of NPEI's Operation, Maintenance and Administration 2015 Test Year spending. There is no reference to conducting, or potentially conducting, a lead-lag study or additional hearing costs - yet SEC seeks to

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<sup>19</sup> Tr. Vol. 1, March 17, 2015, page 67, lines 2 to 15

have NPEI be obligated to incur such expenses. As such, the request is a collateral attack on the Settlement Agreement.

64. NPEI is concerned that the timing of the request comes in submissions following the close of evidence rather than earlier in the hearing process. If the sufficiency of the evidence was such a significant concern for SEC, that a further process was required, it should have been raised earlier in the hearing.

**Summary and Conclusion**

65. NPEI is content to maintain the current fixed-variable split for the residential rate class and would request direction from the Board in respect of the transition to fixed residential billing provided for in the Policy.
66. NPEI requests approval of the 13% working capital allowance. For all of the reasons discussed above, NPEI's request for a 13% working capital allowance should be approved. To depart from the 13% working capital allowance would be arbitrary and without evidentiary support.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

Dated: April 7, 2015	<p><b>AIRD &amp; BERLIS LLP</b> Barristers and Solicitors Brookfield Place 181 Bay Street, Suite 1800 Toronto, Ontario M5J 2T9</p> <p></p> <hr/> <p><b>Scott Stoll</b> (LSUC #45822G) Tel: 416.865.4703 Fax: 416.863.1515</p> <p>Counsel for Niagara Peninsula Energy Inc. ("NPEI").</p>
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