



EB-2014-0301
EB-2014-0072

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 Essex Powerlines Corporation for an order approving a Smart Meter Disposition Rate Rider (SMDR) and a Smart Meter Incremental Revenue Requirement Rate Rider (SMIRR), each to be effective January 1, 2015;

AND IN THE MATTER OF an application by Essex Powerlines Corporation for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2015.

BEFORE: Marika Hare
Presiding Member

Allison Duff
Member

DECISION and ORDER

June 9, 2015

This is the OEB's Decision and Order in the Essex Powerlines Corporation (Essex Powerlines) combined proceeding for its final smart meter installation costs application (EB-2014-0301, the Smart Meter application) and for its annual Price Cap Incentive Rate-Setting adjustment application relating to rates for the 2015 rate year (EB-2014-0072, the Price Cap IR application)¹.

¹ The Smart Meter Application was filed on September 23, 2014 and the Price Cap IR application was filed on September 26, 2014.

Essex Powerlines last appeared before the OEB with a cost of service application for the 2010 rate year in the EB-2009-0143 proceeding. To adjust its 2015 rates, Essex Powerlines selected the Price Cap IR which provides for an adjustment to distribution rates and charges in the period between cost of service proceedings based on inflation, productivity and incentives.

Essex Powerlines' application satisfied the OEB's filing requirements² and, on October 20, 2014, the OEB issued notice that it would hear both applications in a combined proceeding, in writing. OEB staff participated in the proceeding. Initially, only the Vulnerable Energy Consumers Coalition (VECC) applied for, and was granted, intervenor status and cost eligibility. VECC stated that its involvement in the proceeding would be limited to Essex Powerlines' request for the recovery of costs associated with the installation of smart meters.

After the evidentiary phase of the combined proceeding, Essex Powerlines disclosed an error with the evidence filed in the Price Cap IR application. The error related to a misallocation between two Group 1 Deferral and Variance Accounts (DVA); Account 1588 – RSVA Power, and Account 1589 – RSVA Global Adjustment. In its reply submission dated January 20, 2015, Essex Powerlines submitted additional information confirming that it had incorrectly allocated costs in 2011, 2012 and 2013 between Regulated Price Plan (RPP) and non-RPP customers (i.e. those purchasing electricity from a retailer or making individual arrangements for power procurement).

The OEB reopened the record of the proceeding to enable the filing of new evidence and convened an oral hearing to consider the new evidence. Given that there would be a broader potential impact on rates than had been anticipated when the applications were first received, the OEB granted intervenor status and cost awards eligibility to all intervenors of record in Essex Powerlines' last cost of service proceeding³.

In addition to VECC and OEB staff, Energy Probe and School Energy Coalition (SEC) also participated in the combined proceeding. These parties asked interrogatories, attended the oral hearing and made submissions.

² Report of the Board: Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach (October 18, 2012); and Filing Requirements for Electricity Distribution Rate Applications (July 25, 2014)

³ Town of Amherstburg, Town of LaSalle, Municipality of Leamington, and Town of Tecumseh ("Representatives of the Streetlight Class"); Energy Probe Research Foundation ("Energy Probe"); the School Energy Coalition ("SEC"); and the Vulnerable Energy Consumers Coalition ("VECC")

The following issues are addressed in this Decision and Order:

- Rural or Remote Electricity Rate Protection Charge
- Shared Tax Savings Adjustments
- Retail Transmission Service Rates
- Loss of Customers
- Group 1 Deferral and Variance Account Balances
- Consequences of Essex Powerlines' Regulatory Accounting Errors
- Price Cap Index Adjustment
- Debt Servicing Covenants
- Smart Meter Application
- Motion
- Implementation
- Cost Awards

Rural or Remote Electricity Rate Protection Charge

The OEB has determined that the Rural or Remote Electricity Rate Protection (RRRP) benefit and charge for 2015 shall remain at \$0.0013 per kWh⁴. The draft Rate Order filed by Essex Powerlines shall reflect this RRRP charge.

Shared Tax Savings Adjustments

The OEB has determined that a 50/50 sharing of the impact of legislated tax changes between shareholders and ratepayers is appropriate and that the tax reduction will be allocated to customer rate classes on the basis of the OEB-approved distribution revenue from the applicant's last cost of service proceeding⁵.

Essex Powerlines identified a total tax savings of \$157,696 resulting in \$78,848 to be refunded to ratepayers.

The OEB approves the disposition of the shared tax savings of \$78,848 based on a

⁴ Decision with Reasons and Rate Order, EB-2014-0347

⁵ Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors (September 17, 2008)

volumetric rate rider using annualized consumption for all customer classes.

Retail Transmission Service Rates

Electricity distributors are charged for transmission costs at the wholesale level and then pass on these charges to their distribution customers through their Retail Transmission Service Rates (RTSRs). Variance accounts 1584 and 1586 are used to capture differences in the rate that a distributor pays for wholesale transmission service relative to the retail rate that the distributor is authorized to charge when billing its customers.

The OEB has issued guidelines⁶ which outline the information that electricity distributors are to file in order to adjust their RTSRs for 2015. The guidelines require electricity distributors to adjust their RTSRs based on a comparison of historical transmission costs adjusted for the new Uniform Transmission Rates (UTR) and the revenues generated under existing RTSRs. Similarly, embedded distributors, such as Essex Powerlines, must adjust their RTSRs to reflect any changes to the applicable RTSRs of their host distributor, which in this case is Hydro One Networks Inc.

The OEB approved new rates for Hydro One's Sub-Transmission class, including the applicable RTSRs⁷, as shown in the following table:

Table 1: 2015 Sub-Transmission RTSRs

Network Service Rate	\$3.41 per kW
<u>Connection Service Rates</u>	
Line Connection Service Rate	\$0.79 per kW
Transformation Connection Service Rate	\$1.80 per kW

The OEB finds that these 2015 Sub-Transmission class RTSRs are to be incorporated into the filing module to adjust the RTSRs to be charged to customers.

⁶ Guideline G-2008-0001 - Electricity Distribution Retail Transmission Service Rates, revision 4.0 (June 28, 2012)

⁷ Rate Order, EB-2013,0416, issued April 23, 2015

Loss of Customers

Essex Powerlines proposed to remove the consumption data associated with the General Service 3,000 to 4,999 kW rate class in order to calculate the rate riders for deferral and variance accounts, tax savings and RTSR without reallocating any other costs. This rate class had only two customers - Hydro One Networks Inc. which is not charged rate riders as an embedded distributor, and Heinz Corporation which ceased to be a customer in June 2014.

Essex Powerlines analyzed the current usage compared to the latest OEB-approved volumetric forecast and noted that “while all other classes have not changed significantly, the General Service 3,000 to 4,999 kW class has decreased by 100% ... [d]ue to these facts Essex Powerlines has changed the volumetric data used for the General Service 3,000 to 4,999 kW class to ensure the allocation of the tax sharing, deferral and variance and RTSR rate riders are more accurately applied.”

Essex Powerlines considered it appropriate to remove the consumption data; otherwise, a recovery could be approved for a class with no customers. Essex Powerlines indicated that the removal of the Heinz Corporation volumes from the 2013 total consumption reduces the non-RPP portion of the split from 41.23% to 41.00%⁸.

In its submission, OEB staff supported the omission of the consumption data for this customer class and noted the minimal change in the overall percentage.

To calculate rate riders, the Rate Generator Model instructions state:

If there is a material difference between the latest Board-approved volumetric forecast and the most recent 12-month actual volumetric data, use the most recent 12-month actual data.⁹

These options are available because the Rate Generator Model is applied in Price Cap IR applications in which no current consumption forecast is considered. In this Price Cap IR application, the OEB approves Essex Powerlines' proposal to use recent, known information which should reduce any true-up required in the future.

⁸ Undertaking J4, Response, April 21, 2015 (EB-2014-0072/EB-2014-0301)

⁹ Rate Generator Model, Tab 6 – “Billing Det. For Def-Var”

Group 1 Deferral and Variance Account Balances

The OEB's policy on DVAs provides that, during an IRM plan term, a distributor's Group 1 DVA balances will be reviewed and disposed if the preset disposition threshold of \$0.001 per kWh, whether in the form of a debit or credit, is exceeded¹⁰.

As initially filed, Essex Powerlines' 2013 actual year-end total balance of \$1,522,723 for Group 1 DVAs exceeded the disposition threshold. However, when the error was disclosed, it was apparent the evidence was incorrect. Significant balances had been misallocated between the Group 1 Accounts 1588 and 1589.

Accounts 1588 and 1589 in 2011, 2012 and 2013

In its reply submission to the Price Cap IR application, Essex Powerlines included new information relating to an error that it discovered in the 2011, 2012 and 2013 rate years. The source of the error occurred in the settlement forms that Essex Powerlines submitted to the Independent Electricity System Operator's (IESO) which are used to determine the RPP and non-RPP split for the IESO's Global Adjustment and Hydro One Network Inc.'s power billings.

The forms used at that time were the IESO's, and the forms required that Essex Powerlines input an allocation formula that the IESO then used to bill the Global Adjustment. Staff at Essex Powerlines made a data input error in this formula.

The error affected RPP and non-RPP customers as follows¹¹:

Table 2: Annual Breakdown of Misallocated Amounts

	Under-collected from Non-RPP	Over-collected from RPP
2011	\$1,561,164	\$1,561,164
2012	\$3,617,586	\$3,617,586
2013	\$6,419,261	\$6,419,261
Total	\$11,598,011	\$11,598,011

¹⁰ Report of the Board on Electricity Distributors' Deferral and Variance Account Review Initiative (July 31, 2009)

¹¹ Essex Powerlines Response to Procedural Order No. 2, February 11, 2015 (EB-2014-0072/EB-2014-0301)

Essex Powerlines submitted that the error was not previously detected given the volatile nature of Accounts 1588 and 1589. In addition, other Group 1 DVAs were being monitored and, overall, the total balance had not changed significantly. To correct the error, Essex Powerlines proposed an adjustment and re-allocation between RPP and non-RPP customers of approximately \$11.5 million. The proposed accounting adjustments would be a credit to Account 1588 and a debit to Account 1589.

For reasons set out in the OEB's Partial Decision and Procedural Order No. 3 (Procedural Order No. 3), the OEB rejected Essex Powerlines' proposal to correct the misallocation error for rate years 2011 and 2012 totalling \$5,178,750. The OEB found that to do so would constitute retroactive ratemaking as the 2011 and 2012 Group 1 DVA balances were approved on a final basis in Essex Powerlines' 2014 IRM decision.

Despite Procedural Order No. 3, Essex Powerlines in its Argument in Chief, maintained the view that the amounts over and under-billed to customers should be corrected in full (i.e. including the already settled amounts) and submitted that the OEB could correct the error of the misallocation of the riders associated with the disposition of Group 1 DVAs in 2011 and 2012 through application of Rule 41.02 of the *Rules of Practice and Procedure*. In its reply submission, Essex Powerlines indicated that the OEB did not address this argument in Procedural Order No. 3.

This was not an oversight by the OEB in Procedural Order No. 3. The OEB's view was that the application of Rule 41.02 was not applicable in this case. The fact that Essex Powerlines has raised this issue again in its reply submission leads the OEB to question whether Essex Powerlines understands the gravity of its errors.

Rule 41.02 of the *Rules of Practice and Procedure* is used in the case of a minor administrative error. The rule specifically states "The Board may at any time, without notice or a hearing of any kind, correct a typographical error, error of calculation or similar error made in its orders or decisions". To use this rule in the case of Essex Powerlines' allocation of costs associated with Group 1 DVAs would equate the misallocation to a minor error needing correction. The errors made by Essex Powerlines were not minor and impacted its customers in a material way. This does not fall within the category of changes that can be made by the OEB without a hearing.

Accounts 1588 and 1589 Residual Amounts

The 2011 and 2012 Group 1 DVA balances were being disposed through a 2014 rate rider over the May 1, 2014 to April 30, 2015 period. When the error was identified, the OEB issued a Rate Order and ceased the 2014 rate rider, effective February 1, 2015, in order to mitigate any further impacts. Thus, during the last three months of the 2014 rate rider's term (February, March and April 2015) the rate riders were not billed or credited to customers.

With ceasing disposition of the 2014 rate riders for the 2011 and 2012 DVA balances, a residual amount remains in Account 1595 (2014). A large portion of the residual amount is the result of yet-to-be billed February, March and April 2015 consumption and includes amounts related to all Group 1 DVAs (including Accounts 1588 and 1589). In terms of the quantum, Essex Powerlines agreed with OEB staff's calculation to correct the misallocation between Accounts 1588 and 1589 on a dollar-for-dollar basis¹². As of January 31, 2015, the remaining balances are, as corrected over the course of the proceeding and agreed to by Essex Powerlines, a debit in Account 1588 of \$1,198,629 and a credit in Account 1589 of \$1,089,506.

The OEB approves the disposition of the unbilled residual amounts in Account 1595 (2014) of a credit of \$1,020,432 which includes a debit amount of \$1,198,629 in Account 1588 and a credit of \$1,089,506 in Account 1589 (applicable only to Non-RPP customers). The OEB agrees that the residual amounts should be calculated on a dollar-for-dollar basis, considering actual collections to date.

Account 1590 Approved Balance

During the course of the combined proceeding, it was discovered that Account 1590 - Recovered Regulatory Asset Balances was not included in the rate rider calculation of the approved Rate Generator Model in the 2014 IRM proceeding¹³.

Account 1590 had a credit balance of approximately \$1.5 million as at December 31, 2012. The \$1.5 million credit balance was approved by the OEB on a final basis; however, due to a model implementation error, the credit was not included in the rate rider calculations and was not returned to customers.

¹² Oral Hearing Transcript Vol. 1, Page 70 (line 24) to Page 71 (line 7), April 14, 2015 (EB-2014-0072/EB-2014-0301)

¹³ Essex Powerlines Corporation, Reply Submission, March 6, 2015, Page 4 (EB-2014-0072/EB-2014-0301)

In Procedural Order No. 3, the OEB directed the utility to bring this amount forward along with its Group 1 DVAs as at December 31, 2013 for disposition over a one-year period commencing May 1, 2015 (see OEB findings in Implementation section).

Group 1 DVA Balances as at December 31, 2013

Essex Powerlines provided an updated DVA continuity schedule for the requested disposition of its 2013 Group 1 DVAs with no adjustment to the 2011 and 2012 balances in Accounts 1588 and 1589 (as per Procedural Order No. 3) and with the correcting adjustments to the 2013 balances only to Accounts 1588 and 1589. The updated continuity schedule included Account 1590¹⁴.

Essex Powerlines proposed the following disposition periods:

- Group 1 DVAs, excluding Accounts 1588 and 1589: one-year period commencing May 1, 2015
- Account 1588: two-year period commencing May 1, 2015
- Account 1589: four-year period commencing May 1, 2015

The OEB approves the Group 1 DVA balances as at December 31, 2013 on an interim basis. This balance excludes the 2013 balances in Accounts 1588 and 1589, and includes Account 1590 and 1595 (2014). In the Implementation section of this Decision and Order, the OEB approves a June 1, 2015 effective and implementation date for 2015 rates. As a result, the OEB approves an 11-month disposition period from June 1, 2015 to April 30, 2016.

The OEB approves the disposition of the 2013 balances in Account 1588 of a \$2,151,411 credit and in Account 1589 of a \$4,382,923 debit on an interim basis. The OEB approves a 23-month disposition period for the credit or refund to customers of the Account 1588 balance and a 35-month disposition period for the debit or charge to customers of the 1589 balance. The draft Rate Order should consider the revised bill impact on customers.

¹⁴ Essex Powerlines, Updated Rate Generator Model "Essex Powerlines_2015 IRM_Rate_Generator_Appendix A Master Exhibit 1_20150407", April 7, 2015

Table 3 provides the amounts that Essex Powerlines should use in calculating the necessary rate riders and disposition periods.

Table 3: Amounts Applicable for Each Rate Rider Calculation

	\$	Disposition Period
Rate Rider 1		
2013 Balances (includes 1590 and 1595 (2014) residuals for all Group 1 accounts, excluding Accounts 1588 and 1589 for the 2013 balances)	(4,400,946)	
Account 1595 (2014) - Account 1588 residual	1,198,629	
Total	(3,202,317)	11-months
Rate Rider 2 (applicable only to Non-RPP customers)		
Account 1595 (2014) - Account 1589 residual	(1,089,506)	11-months
Rate Rider 3		
Account 1588 (2013)	(2,151,441)	23-months
Rate Rider 4 (applicable only to Non-RPP customers)		
Account 1589 (2013)	4,382,923	35-months

The balance of each Group 1 DVA approved for disposition shall be transferred to the applicable principal and interest carrying charge sub-accounts of Account 1595. Such transfer shall be pursuant to the requirements specified in Article 220, Account Descriptions, of the Handbook. The date of the transfer must be the same as the effective date for the associated rates. Essex Powerlines should ensure these adjustments are included in the reporting period ending June 30, 2015 (Quarter 2).

Consequences of Essex Powerlines' Regulatory Accounting Errors

In its Procedural Order No. 3, the OEB stated that, in situations where errors are the result of a utility's negligence, the OEB could impose financial or other consequences on the utility.

OEB staff submitted that Essex Powerlines has the ultimate control over its books and is responsible for ensuring that it follows the OEB's Accounting Procedures Handbook (the Handbook)¹⁵ and ensuring the accuracy of its filings with the OEB. OEB staff submitted that in this case, Essex Powerlines has not met its responsibility to do so. In OEB staff's view, systemic carelessness towards ensuring proper regulatory accounting should be met with serious consequences; and, the result of such consequences should benefit customers who have been materially harmed through no fault of their own. OEB staff submitted if a financial consequence is applied as a result of the errors, it should be a 300 basis point reduction in the regulatory Return on Equity (ROE) embedded in rates to 6.85%, for a two-year period commencing May 1, 2015. OEB staff used Essex Powerlines' 2013 regulatory ROE calculation to estimate the amount it would forego based on a return of 6.85%. OEB staff estimated this amount to be approximately \$550,000 per year.

VECC submitted that the penalty paid by Essex Powerlines should result in Essex Powerlines' RPP customers being made whole unless there is evidence that this would have an adverse impact on the financial viability of the utility. VECC noted that extending the penalty over a number of years would mitigate the effects upon the utility.

SEC submitted that the over-collected amounts from RPP customers should be refunded and that the OEB should exercise its discretion and order Essex Powerlines to credit RPP customers.

Energy Probe submitted that an error resulting in one group of customers benefitting at the expense of another group of customers is not an appropriate outcome. However, if the OEB rejects Essex Powerlines' proposal to correct the misallocation again, Energy Probe submitted that the OEB should impose a penalty on the utility in order to compensate RPP customers. Energy Probe suggested that Essex Powerlines could finance the refund in a number of ways.

The OEB notes that parties used various terms to describe the proposed consequence that should be imposed on Essex Powerlines for its regulatory accounting errors. These

¹⁵ Accounting Procedures Handbook for Electricity Distributors (Effective January 1, 2012)

include a penalty¹⁶, an award of damages for negligence¹⁷, an exercise of the OEB's discretion¹⁸, and as a debit toward Essex Powerlines' return on equity.¹⁹

In its reply, Essex Powerlines submitted that the analysis of imposing a penalty is much more complex than portrayed by parties to this proceeding. The proposed payment ranged from \$1.1 million (OEB staff) to \$3.7 million (VECC, SEC and Energy Probe).

Essex Powerlines submitted that the OEB's only power to order penalties is in Part VII.1 of the *Ontario Energy Board Act, 1998* which addresses compliance. Further, Essex Powerlines submitted that there is nothing in the legislation to suggest that the OEB has the power to impose penalties in any other circumstances. Essex Powerlines also submitted that there is no legal basis for the argument that the OEB has discretion to make an ROE adjustment given a utility made an error.

The OEB has considered the evidence with respect to the issue of negligence versus careless accounting and whether or not a financial consequence should be paid by the shareholder of Essex Powerlines as a result. The OEB has also considered the submissions of Essex Powerlines that the OEB's only power to order penalties is through a compliance proceeding.

The OEB finds that based on the evidentiary record, Essex Powerlines demonstrated carelessness towards ensuring proper regulatory accounting procedures and controls.

Regulatory Accounting Procedures and Controls

It is imperative that electricity distributors adhere to the Handbook. The Handbook is a fundamental pillar for regulatory accounting in Ontario, and the Uniform System of Accounts provides the structure on which the Handbook is based. With 70 electricity distributors, the Handbook and related guidance ensure consistency and comparability of accounting treatments, regulatory books and the resulting rates.

During the course of the combined proceeding, numerous examples of Essex Powerlines not adhering to the Handbook and the Uniform System of Accounts became evident. One example was the credit balance in Account 1590 that had not been

¹⁶ Energy Probe, Submission, Page 4, April 30, 2015 (EB-2014-0072/EB-2014-0301)

¹⁷ VECC, Submission, Pages 4-5, April 30, 2015 (EB-2014-0072/EB-2014-0301)

¹⁸ SEC, Submission, Page 3, April 30, 2015 (EB-2014-0072/EB-2014-0301)

¹⁹ OEB staff Submission, Pages 13-14, April 30, 2015 (EB-2014-0072/EB-2014-0301)

disposed. Evidence was filed indicating that Account 1590 should not have had any balance in 2014. In guidance issued in August 2008²⁰, the OEB clearly instructed distributors that post-April 30, 2008, new balances were to be brought forward to Account 1595 for approval and disposition. Essex Powerlines did not follow this instruction. This is not acceptable.

In addition, the OEB is very concerned about the regulatory accounting controls in place. The fact that Essex Powerlines is a small distributor in terms of customer numbers and staff is no excuse for not implementing all accounting practices properly with sufficient review and oversight. Regardless of size, all Ontario distributors must establish controls to mitigate the risk of error or omission. These controls include the record keeping for Group 1 DVAs.

Distributors are required to settle Group 1 DVAs, including the cost of power and Global Adjustment between the IESO and its distribution customers. The OEB expects management to provide adequate controls and oversight, commensurate with the millions of dollars that flow through Group 1 DVAs, in particular Accounts 1588 and 1589.

Unfortunately this proceeding devolved, in large part, into a forensic accounting exercise in which the OEB found it necessary to ask two sets of supplemental questions through procedural orders, in order to understand the evidence and clarify the record. Moreover, considerable resources were required by the OEB and the parties to decipher the three sets of continuity schedules filed after the interrogatory phase of the proceeding.

As a result of these concerns, the OEB orders that a complete audit of all DVA accounts, procedures and controls be undertaken. The only exceptions are the smart meter Accounts 1555 and 1556 which have undergone a final review in this proceeding. The audit will ensure all DVA entries and balances, not just those associated with Group 1 variance accounts, are accurate for 2013 and on a go forward basis.

Essex Powerlines will pay for the OEB's costs to conduct the audit of all DVA accounts.

²⁰ Ontario Energy Board Accounting Procedures Handbook Frequently Asked Questions, August 2008

The OEB's Audit and Performance Assessment Group conducts utility audits as part of its oversight responsibility of licensed distributors. The cost of conducting the audits are usually included and recovered with other OEB operating costs.

As part of the OEB's audit program, an audit of Essex Powerlines' Group 2 deferral and variance accounts was conducted recently. In the audit report dated March 28, 2013, Essex Powerlines had been cited for a number of incorrect regulatory accounting entries and procedures²¹.

A second audit, within two years, is not normal business practice for the OEB's audit group and extends beyond the OEB's typical oversight responsibility. The need for a second audit is a result of the quality of the evidence in this proceeding.

The OEB's invoice for the audit costs will be provided to Essex Powerlines upon completion of the audit and issuance of the audit report. All audit costs are to be borne by the shareholder, none from its customers.

Price Cap Index Adjustment

The Price Cap IR option is a streamlined regulatory process. Under the Price Cap IR methodology²², distribution base rates are adjusted by an inflation factor, less the sum of a productivity factor and a stretch factor. Based on its established method²³, the OEB has set the inflation factor for 2015 rates at 1.6% and the productivity factor at zero percent. Based on the analysis of the OEB's consultant, Pacific Economic Group (PEG), the stretch factor is assigned based on a distributor's cost evaluation ranking, and ranges from 0.0% to 0.6%. This stretch factor ranking is indicative of a distributor's cost performance relative to other distributors in Ontario. What this means is that the most efficient distributor, based on the cost evaluation ranking, would be assigned the lowest stretch factor of 0.0%.

In this case, the OEB denies this aspect of the application made by Essex Powerlines for a base rate increase based on the Price Cap IR formula. The increase would have

²¹ Exhibit K2 -Audit Review of Group 2 Deferral and Variance Accounts, March 28, 2013 (EB-2014-0072/EB-2014-0301)

²² Report on Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors (December 4, 2013)

²³ As outlined in the Report cited at footnote 2 above.

generated approximately \$160,000 in additional revenue based on Essex Powerlines' placement in the second stretch-factor cohort.

The OEB is required to set just and reasonable rates and in doing so it must balance the interests of the utility and its customers. The Price Cap IR option is predicated on an outcomes-based approach, designed to incent the utility and provide value to customers. As evidenced in this proceeding, with the errors made, the OEB finds that Essex Powerlines has neither demonstrated the desired outcomes nor provided value to its customers. The OEB has therefore determined that maintaining base rates at the same level for 2015, with no increase, is appropriate in the circumstances. The base rates declared interim as of May 1, 2015 are now declared final, with the exception of the rate riders for the Group 1 DVAs.

Debt Servicing Covenants

In transcript undertaking response²⁴ and in reply submission, Essex Powerlines indicated that any financial consequence in excess of \$380,000 would put Essex Powerlines off-side of its debt servicing covenants. In a Price Cap IR application, a distributor's financing structure is not in scope. However, the OEB will not ignore the evidence or submissions filed on this subject.

Essex Powerlines submitted that "any impact that would knowingly and intentionally put a utility off-side of its loan agreements would be contrary to the OEB's statutory objective of maintaining a financially viable industry".

The OEB is very concerned with the apparent risks assumed by Essex Powerlines in structuring its debt arrangements and the subsequent, thin margin of risk it can absorb. Even normal business risks associated with changes in weather and customer demand could represent a high risk to Essex Powerlines and expose it to risk of default.

The OEB agrees with SEC's submissions that a distributor should not structure its debt covenants such that a reduction of 150 to 200 basis points in actual return on equity would put the distributor in a position of default. As a point of comparison, the OEB's own guideline for a financial review is triggered by a return variation of 300 basis points.

²⁴ Transcript Undertaking Response J3 and Supplemental Response filed by Essex Powerlines (EB-2014-0072/EB-2014-0301)

As a result, consistent with the OEB's statutory objective, the OEB recommends that at its next cost of service application, Essex Powerlines file sufficient information to enable the OEB to fully review the inherent risks of its financing arrangements.

Smart Meter Application

Costs Incurred for Smart Meter Deployment and Operation

In the Smart Meter Application, Essex Powerlines sought the following approvals:

- Smart Meter Disposition Rider (SMDR) – rate rider of (\$1.15) per Residential customer per month and \$10.49 per General Service less than 50kW customer per month, effective January 1, 2015.
- Smart Meter Incremental Revenue Requirement Rate Rider (SMIRR) – rate rider of \$1.11 per Residential customer per month and \$3.81 per General Service less than 50kW customer per month effective January 1, 2015.

Essex Powerlines requested that the SMDRs and SMIRRs be in effect for a 12-month period. In response to OEB staff interrogatories, Essex Powerlines made corrections for the following:

- Addition of capital and OM&A actual costs for 2012 and 2013 and forecasted costs for 2014 and 2015 (OEB staff IR #10b);
- Corrected tax rates (OEB staff IR #16);
- Re-submitted Smart Meter Model v.5.0 (applicable for 2015 applications). Essex Powerlines has originally submitted version 4.0, applicable for 2014 rate applications (OEB staff IR #17); and
- Revised effective dates and recovery periods for the SMDRs and SMIRRs (OEB staff IR #18), so that the effective date would be May 1, 2015, corresponding with the proposed effective date of revised base distribution rates per the Incentive Rate Regulation application, and with changed recovery periods to mitigate rate impacts, particularly for General Service <50 kW customers.

In addition, Essex Powerlines filed a revised Smart Meter Model and class-specific SMDRs and SMIRRs to reflect changes noted in OEB staff interrogatories. However, in its submission, OEB staff noted that Essex Powerlines made input errors in the revised

Smart Meter Model which corrupted some of the calculations. OEB staff attempted to correct the calculation errors, and provided a revised smart meter model for review as part of its submission.

In its reply submission, Essex Powerlines filed a further revised Smart Meter Model and proposed class-specific SMDRs and SMIRRs to reflect the corrections to the errors noted above. Essex Powerlines also noted that it corrected the percentage split error for Residential and General Service<50kW on tabs 10A and 10B of the Smart Meter Model which OEB staff referenced in its submission. OEB staff noted that the meter cost for capital allocated to the Residential rate class was 80% and the General Service rate class was 22%, totaling 102%. Essex Powerlines, in its reply submission, verified the correct percentages attributable to these rate classes, totaling 100%. The following tables reflect all relevant corrections filed on the record:

Table 4: Original and Revised SMDRs and SMIRRs for Residential Rate Class

Rate Rider	Per Original Application		Revised for Interrogatory Responses		As Per OEB staff Revised Model		As per Essex Powerlines' Reply Submission	
	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)
SMDR	January 1, 2015	(\$1.15)	May 1, 2015	\$(0.04)	May 1, 2015	\$(0.04)	May 1, 2015	\$(0.04)
SMIRR	January 1, 2015	\$1.11	May 1, 2015	\$1.07	May 1, 2015	\$1.07	May 1, 2015	\$1.07

Table 5: Original and Revised SMDRs and SMIRRs for General Service<50kW

Rate Rider	Per Original Application		Revised for Interrogatory Responses		As Per OEB staff Revised Model		As per Essex Powerlines' Reply Submission	
	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)	Proposed Effective Date	Amount (\$/month)
SMDR	January 1, 2015	\$10.49	May 1, 2015	\$15.53	May 1, 2015	\$9.32	May 1, 2015	\$8.20
SMIRR	January 1, 2015	\$3.81	May 1, 2015	\$3.80	May 1, 2015	\$3.80	May 1, 2015	\$3.46

The following table summarizes Essex Powerlines' overall per meter costs, costs above minimum functionality and capital and OM&A expenses:

Table 6: Average Capital Cost Per Meter

Smart Meter Capital Costs, Including Costs Exceeding Minimal Functionality	\$3,354,090
Remove Smart Meter Capital Costs Exceeding Minimal Functionality	(\$3,791)
Smart Meter Capital Costs, Excluding Costs Exceeding Minimal Functionality	\$3,350,299
Number of Meters Installed	28,775
Average Capital Cost per Meter, Excludes Costs Exceeding Minimum Functionality	\$116.43

Table 7: Average Total Cost Per Meter

Smart Meter Total Costs, Including Costs Exceeding Minimal Functionality	\$3,519,105
Remove Smart Meter Total Costs Exceeding Minimal Functionality	(\$34,232)
Smart Meter Total Costs, Excluding Costs Exceeding Minimal Functionality	\$3,484,873
Number of Meters Installed	28,775
Average Total Cost per Meter, Excludes Costs Exceeding Minimum Functionality	\$121.11

On March 3, 2011, the OEB issued the Monitoring Report, Smart Meter Investment – September 2010 (“the Monitoring Report”). The Monitoring Report showed an average cost of \$226.92 per smart meter. OEB staff submitted that Essex Powerlines' costs are below the average costs identified in the Monitoring Report and therefore, took no issue with the nature and quantum of Essex Powerlines' reported per meter costs.

VECC noted that Essex Powerlines' costs compare favourably as they are below the sector average of \$186.76 capital cost per meter and \$207.37 total cost per meter (based on September 2009 data)²⁵ and the total cost per meter of \$226.92 (based on September 2010 data)²⁶.

²⁵ “Sector Smart Meter Audit Review Report”, dated March 31, 2010

²⁶ Monitoring Report Smart Meter Investment – September 2010, March 3, 2011

Essex Powerlines' application included a request to recover \$3,791 in capital costs and \$30,441 in OM&A costs beyond minimum functionality, as defined in the combined proceeding related to Smart Meters (EB-2007-0063). These costs include CIS system upgrades, TOU implementation, web presentment, bill presentment and integration with MDM/R. Neither VECC nor OEB staff took issue with the nature or quanta of Essex Powerlines' documented costs for beyond minimum functionality based on the documentation and explanations provided in evidence.

The OEB notes that authorization to procure and deploy smart meters has been done in accordance with Government regulations, including successful participation in the London Hydro RFP process, overseen by the Fairness Commissioner, to select (a) vendor(s) for the procurement and/or installation of smart meters and related systems.

The OEB finds that Essex Powerlines' documented costs, as revised in response to interrogatories and in its reply submission, related to smart meter procurement, installation and operation, and including costs beyond minimum functionality, are reasonable. The OEB approves the recovery of the costs for smart meter deployment.

In granting its approval for the historically incurred costs and the incremental annual revenue requirement, the OEB considers Essex Powerlines to have completed its smart meter deployment. Going forward, Essex Powerlines is not to record any capital and operating costs for existing and new smart meters in Accounts 1555 and 1556. Instead, the costs shall be recorded in regular capital and operating expense accounts (e.g. Account 1860 for meter capital costs) as is the case with other regular distribution assets and costs.

Essex Powerlines is authorized to continue to include the gross book value and accumulated depreciation of stranded meters in the appropriate sub-account of Account 1555. The gross book value and accumulated depreciation balance for stranded conventional meters, as well as the costs currently embedded in Essex Powerlines' approved distribution rates for conventional meters, should be brought forward for disposition in Essex Powerlines' next cost of service application or in a separate application within three years of the date of this Decision and Order, whichever occurs first.

Allocation of Smart Meter Costs

Essex Powerlines applied for class-specific SMDRs and SMIRRs for the Residential and General Service<50 kW customer classes based on an allocation methodology approved in the PowerStream application, EB-2010-0209.²⁷ Essex Powerlines allocated costs using the following method:

- Capital costs related to smart meters is allocated on the basis of customer weighted meters;
- OM&A is allocated on the basis of the number of smart meters; and
- PILs is allocated on the basis of the revenue requirement before PILs by class.

In its submission, VECC noted the average cost of an installed smart meter for a General Service<50 kW customer is approximately three times greater than the cost to install a smart meter for a residential customer. VECC submitted that, to avoid undue cross subsidy between customer classes, Essex Powerlines should calculate class-specific rate riders that reflect the full costs for each customer class. VECC accepted that Essex Powerlines does not have the cost data by rate class to complete separate smart meter models by customer class based on full cost causality. VECC also accepted Essex Powerlines' cost allocation methodology as a proxy for revenue requirement with one exception, as explained below.

VECC submitted that Essex Powerlines collected the smart meter funding adder revenue from classes other than Residential and General Service<50 kW. VECC took issue with Essex Powerlines' approach to reallocate the costs to the residential customer class (93.5%) and General Service<50 kW customer class (6.5%). Essex Powerlines had argued that the amounts are not significant based on the overall revenues collected. VECC submitted that as a matter of principle, the SMFA revenues collected from other rate classes should be returned instead of the allocation proposed by Essex Powerlines.

Essex Powerlines did not address this matter in its reply submission.

²⁷PowerStream, Application, page 16 (EB-2010-0209)

As indicated in the Waterloo North Hydro Inc.'s Smart Meter Cost Recovery Application decision (EB-2012-0266):

The Board notes that VECC has made a similar submission in other applications for recovery of smart meter costs, beginning with PowerStream's 2010 smart meter application. In prior cases, the Board has not accepted VECC's proposal to return SMFA revenues to metered customer classes that do not receive smart meters, and will not do so with respect to this Application. As stated in prior decisions, larger demand-metered customers may benefit from the universal deployment of smart meters and implementation of TOU rates to lower consumption customers, and the Board views that the amounts are not material on per customer basis²⁸.

The OEB notes the concerns of VECC, and concurs that the cost differential per meter may be larger than has been experienced in many other smart meter cost recovery applications. The OEB observes that this is not surprising based on the evidence. Essex Powerlines documented that 956 General Service<50 kW customers installed 3-phase smart meters at an average installed cost of \$648.96 per meter versus 1,056 General Service<50 kW customers receiving single-phase smart meters at \$121.37. 26,795 Residential customers received single-phase smart meters at an average installed cost of \$104.17. The OEB finds that Essex Powerlines has correctly applied the accepted cost allocation methodology based on the evidence.

The OEB finds that the allocation of costs in the Smart Meter Application is consistent with the Waterloo North and PowerStream decisions and is therefore approved. As stated in prior decisions, larger demand-metered customers may benefit from the universal deployment of smart meters and implementation of TOU rates to lower consumption customers, and the OEB views that the amounts are not material on per customer basis.

Stranded Meter Accounting

Essex Powerlines proposed not to dispose of stranded meters at this time, but to deal with disposition in its next rebasing application, scheduled for 2016 rates. The estimated net book value of the stranded meters as of December 31, 2015 is

28 EB-2012-0266, Decision and Order, Page 5

\$1,567,710.²⁹ The stranded conventional meters continue to be amortized until disposition. Based on the number of installed smart meters, approximately 28,000, the estimated net book value per stranded conventional meter is about \$55.

OEB staff submitted that Essex Powerlines' proposal is in accordance with Guideline G-2011-0001. OEB staff noted that, at the time of Essex Powerlines' next rebasing application, Essex Powerlines should make a proposal for allocating the net book value of stranded meters to the Residential and General Service<50 kW classes. OEB staff observes that a standard approach approved by the OEB in recent proceedings is to use the ratio of installed conventional meter costs by customer class from sheet I7.1 of the Cost Allocation model as found in the distributor's most recent cost of service application. Essex Powerlines should consider this, or a similar approach for requesting disposition and recovery via class-specific Stranded Meter Rate Riders in its forthcoming cost of service application.

The OEB agrees with the submission of OEB staff.

Effective Date and Duration of Smart Meter Rate Riders

Essex Powerlines' requested an effective date of May 1, 2015 and a 12-month disposition period for its SMDR and SMIRR.

In the Implementation section of this Decision and Order, the OEB approves a June 1, 2015 implementation and effective date for 2015 rates. As a result, the OEB approves an 11-month disposition period from June 1, 2015 to April 30, 2016 for the SMDR and SMIRR.

Motion

Essex Powerlines filed a motion (the Motion) to review and vary, suspend or cancel certain portions of Procedural Order No. 3³⁰. The OEB issued Procedural Order No. 4, and ordered that the Motion be placed in abeyance to permit the OEB to complete the

²⁹ Essex Powerlines, Interrogatory Responses, Board Staff IR #11 (EB-2014-0072/EB-2014-0301)

³⁰ Essex Powerlines Corporation, Notice of Motion, April 2, 2015 (EB-2014-0072/EB-2014-0301)

record of the current proceeding and preserve Essex Powerlines' right to file a dispositive motion if it so chooses³¹.

Implementation

The OEB has made findings in this Decision and Order which change the 2015 distribution rates from those proposed by Essex Powerlines. The OEB expects Essex Powerlines to file a draft Rate Order, including a proposed Tariff of Rates and Charges and all relevant calculations showing the impact of this Decision and Order on Essex Powerlines' determination of the final rates. The draft Rate Order will be based on a June 1, 2015 effective and implementation date.

In its draft Rate Order, Essex Powerlines should consider the bill impacts on customers, and should address any situations that might require mitigation appropriately. Essex Powerlines should provide adequate supporting documentation in its draft Rate Order including, but not be limited to, a completed version of the 2015 IRM Rate Generator model and Smart Meter Model, and estimated bill impacts for representative customer profiles in all customer classes.

A Rate Order will be issued after the steps set out below are completed.

THE ONTARIO ENERGY BOARD ORDERS THAT:

1. Essex Powerlines shall file a draft Rate Order that includes revised models in Microsoft Excel format and a proposed Tariff of Rates and Charges reflecting the OEB's findings in this Decision by June 12, 2015.
2. Any comments on the draft Rate Order including the revised models and proposed rates with the OEB and forward to Essex Powerlines by June 16, 2015.
3. Essex Powerlines shall file responses to any comments on its draft Rate Order including the revised models and proposed rates by June 18, 2015.

³¹ Essex Powerlines Corporation, Procedural Order No. 4, April 10, 2015 (EB-2014-0072/EB-2014-0301)

COST AWARDS

The OEB finds that the costs of this proceeding, including OEB costs, intervenor costs and Essex Powerlines' own legal and any other external costs are to be borne by the utility's shareholder.

The OEB will issue a separate decision on cost awards once the following steps are completed:

1. Intervenors shall submit its cost claims no later than 7 days from the date of issuance of the final Rate Order.
2. Essex Powerlines shall file with the OEB and forward to intervenors any objections to the claimed costs within 17 days from the date of issuance of the final Rate Order.
3. Intervenors shall file with the OEB and forward to Essex Powerlines any responses to any objections for cost claims within 24 days from the date of issuance of the final Rate Order.
4. Essex Powerlines shall pay the OEB's costs incidental to this proceeding upon receipt of the OEB's invoice.

All filings to the OEB must quote the file numbers EB-2014-0301 and EB-2014-0072 and be made electronically through the OEB's web portal at www.pes.ontarioenergyboard.ca/eservice/ in searchable / unrestricted PDF format. Two paper copies must also be filed at the OEB's address provided below. Filings must clearly state the sender's name, postal address and telephone number, fax number and e-mail address. Parties must use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at www.ontarioenergyboard.ca/OEB/Industry. If the web portal is not available parties may email their documents to the address below. Those who do not have internet access are required to submit all filings on a CD in PDF format, along with two paper copies. Those who do not have computer access are required to file 7 paper copies.

All communications should be directed to the attention of the Board Secretary at the address below, and be received no later than 4:45 p.m. on the required date.

ADDRESS

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto ON M4P 1E4
Attention: Board Secretary
E-mail: boardsec@ontarioenergyboard.ca
Tel: 1-888-632-6273 (Toll free)
Fax: 416-440-7656

DATED at Toronto, June 9, 2015

ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary