London Hydro
111 Horton Street
P.O. Box 2700
London, ON
N6A 4H6

July 9, 2015

Ms. Kirstin Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Re: Consultation on the Regulatory Treatment of Pensions and Other Post-Employment Benefit Costs Board File Number EB-2015-0040

Dear Ms. Walli:

London Hydro herein submits our submission with respect to the OEB's Consultation on the Regulatory Treatment of Pensions and Other Post-Employment Benefit Costs Board File Number EB-2015-0040

Yours Truly,

Martin Benum
Director of Regulatory Affairs
London Hydro
Tele: 519-661-5800 ext. 5750
Cell: 226-926-0959
email: benumm@londonhydro.com

General Principles

1. What principles should the OEB adopt in addressing pension and OPEB issues?

Potential principles include: consistency across the gas and electricity sectors; intergenerational equity; financial protection for future ratepayers; ensuring the most efficient level of costs for ratepayers; stable cost levels; pension costs which are comparable as measured by other benchmarks, etc.

London Hydro is fortunate to be a member of the OMERS pension plan program, which has been the central program for Ontario municipal based members. Established in 1962, OMERS provides defined pension benefits to local government employees, retirees and beneficiaries throughout Ontario. The OMERS Primary Pension Plan is a jointly sponsored, multi-employer pension. Primary Plan employers range from large cities, to numerous local agencies. Primary Plan members include union and non-union municipal workers; police, firefighters and paramedics; the non-teaching staff of school boards; and employees of children's aid societies, transit systems and electrical utilities. London Hydro would suggest there is sufficient consistency across most municipal based electrical utilities who are members of OMERS.

London Hydro recognizes that OMERS is susceptible to volatility resulting from a myriad of influences (economic market changes, longer life spans, etc.). While London Hydro believes that this cannot be controlled by any power, at least it is relatively consistent among member utilities.

Hence London Hydro would suggest that with respect to OMERs pensions the municipal electricity sector utilities have currently achieved consistency across the OMER member sector resulting in a reasonable level of intergenerational equity; financial protection for future ratepayers; ensuring the most efficient level of costs for ratepayers; stable cost levels; and pension costs which are comparable as measured.

London Hydro expresses no opinion with respect to non-OMERS based pension plans.

London Hydro OPEB plans are historically driven primarily by local union member contract negotiation. Typically, the benefit settlements resulting from these negotiations are extrapolated to all employees of the utility for fairness. Normally these contract negotiations are local in nature but are usually influenced by the results of settlements derived in other comparable jurisdictions, which provides for effective benchmarking. The attraction and retention of strong candidate employees to the utility can dictate some alternation from the norm, but for the most part municipal based electrical utilities have sufficient consistency amongst its peers.

Again, London Hydro recognizes that OPEBs are highly susceptible to volatility resulting from a myriad of influences (economic market changes, longer life spans, etc.). While London Hydro believes that this cannot be controlled by any power, at least it is relatively consistent among like municipally based utilities.

One issue experienced by London Hydro results from legacy OPEB contracts that carry forward. This is detailed further in our application made to the OEB in 2014 (EB-2014-0196). This issue highlights one of the biggest challenges faced by utilities such as London Hydro. London Hydro principal problem is that it cannot undo the past. With benefit carriers facing increasing risks, their cost requirements for covering our legacy OPEB contract have been escalating with each carrier negotiation. Further we have seen fewer benefit carriers competing for coverage of our legacy programs, to the point where London Hydro may have to self-fund this program if no carrier offers coverage. This has significant impact on the OPEB actuarial reviews and hence will influence cost requests in future cost of service application.

London Hydro proposed to the OEB in our application, described above, for an opportunity to explore alternatives solutions designed to reduce higher future costs. It was felt London Hydro could prevent some intergenerational inequity by charging current customers now versus charging future customers with higher past costs. Unfortunately the Board denied our proposal. As an act of financial prudence and risk aversion, our Board of Directors had no alternative but to hold status quo and continue on our current uncertain path. London Hydro would recommend that one guiding principle for the OEB to consider is for the Board to be more open minded in allowing utilities avenues to pursue opportunities outside of the normal scope of business.

If London Hydro were a private enterprise the decision to pursue our proposed solution would have been most likely accepted by our Board of Directors, as it had the potential as a prudent decision. However as a regulated utility the view of prudent action by our Board of Directors is forced to be holding the status quo and allow creeping costs into future cost of service applications.

Otherwise London Hydro would suggest that with respect to OPEBs the sectors current methodology inherently has achieved consistency across the municipal member electricity sectors; has a reasonable level of intergenerational equity; does provide reasonable financial protection for future ratepayers; ensures the most efficient level of costs for ratepayers; provides reasonable stable cost levels; and OPEB costs which are comparable through comparing union settlement agreements.

London Hydro expresses no opinion with respect to non-municipal based OPEB plans.

2. Are there other types of costs previously considered by the OEB that provide suitable analogies for the consideration of pension and OPEB issues?

(for example: deferred taxes; asset retirement obligations; site restoration costs)

London Hydro sees no other types of costs considered by the OEB as being directly comparable. The issue at hand for these costs is the volatility of external influences such as the economy, rising health care costs, changes in life expectancy.

Information Requirements

3. Should the applicants be required to compare their pension and OPEB costs to industry norms and/or other benchmarks?

(Note: It is the OEB's expectation that the next phase of the consultation will consider the development of a complete set of new or incremental information that should be filed in applications seeking cost recovery for pensions and OPEBs).

London Hydro has suggested that most Ontario municipal based electrical utilities are members of OMERS and therefore OMERS provisions would be the industry norm.

For OPEB there is natural consideration based on the obtainment of other agreements for collective bargaining purposes. Obviously there is some influence by local management in the interest of attracting, obtaining and retaining quality employees.

By its own nature the influence of the incentive rate making mechanism drives the efficiency for design and containment of OPEB's.

The difficulty with establishing a benchmark for OPEB's would be in the consideration of intangibles such as diversity of employee age and gender; attractiveness of area of operation ; and other influences.

4. What other relevant information should the Board evaluate in order to effectively assess the pension and OPEB costs that a rate-regulated entity is seeking to be included in the rates charged to customers?

London Hydro would suggest that municipally based utilities presently file sufficient information in cost of service (COS) applications to determine whether the pensions and OPEB costs are reasonable.

For the most part OMERS costs are formulaically calculated and can be justified by mathematical calculation. This is an easily tested application.

The ability of the utility to demonstrate that the OPEB obligations and costs are sustainable and will not create undue pressure on ratepayers in the future is a little more complicated to test. Generally however actuarial information filed in COS applications, and normally updated every three years, should provide the information necessary to assess whether OPEB obligations are sustainable.

The OEB has access to the publically filed actuarial information from previously filed applications that could garner the comparability required to test an applicants submission.

Accounting and Recovery in Rates

5. a) Should the OEB establish accounting and recovery methods for both the electricity and gas sectors?

London Hydro wishes to only address issues related to municipal based electricity distributors.

London Hydro would suggest that there is no need to change the current IFRS based pension accounting or recovery methods for municipally based utilities under OMERS as the current approach is working reasonably.

Likewise for OPEB, the current IFRS based accounting and recovery methods for municipally based utilities are the current approach accepted by the OEB. While there are inherent reporting fluctuations as a result of the IFRS based accounting methodology, this is reasonably close to the previous CICA standard 3461. London Hydro adopted CICA 3461 as of January 1, 2000.

London Hydro would suggest that the OEB has adopted the IFRS standard for accounting and that it would not be in the interest of all concerned to detract to far from that methodology as it creates confusion in financial reporting and market comparison.

b) What criteria should be considered to determine the appropriate approach?

London Hydro would suggest that the appropriate approach for most municipally based utilities under OMERs is to continue to use the current IFRS accounting basis. For the most part OMERs costs are a component of employee compensation and formulaically derived. The details for application percentage are publically available, and detailed calculations can be provided in a COS application. This long standing approach has been generally accepted by the OEB.

As OPEB's are a form of deferred compensation earned by employees for the services that they provide during their working years, the costs of providing those benefits should be properly included as a liability whose annual accrual expense is included in a COS during the period that the benefits are earned. The difficulty with OPEBs is that they are normally assigned to a benefit carrier whose assumes the risk of coverage for a quoted period of duration. This coverage is reviewed periodically and costs often re-set. The employee base of a utility stratifies a wide spectrum of age and gender. Third party actuarial evaluation has become the prima fascia methodology for valuation. This approach has been generally accepted by the OEB and the general accounting world at large.

c) If one method is adopted, what should it be: cash (pay-as-you-go) basis, funding contribution basis, accrual (accounting cost) basis or another method?

(please provide details)

- "Pay-as-you-go" cash payment: is equal to the benefit payment to the plan beneficiaries, as specified by the terms of the plan
- Funding contribution: the minimum amount of contribution required to be made by a sponsor of a registered pension plan that is subject to the requirements of pension legislation in Ontario under the Pension Benefits Act, Ontario (PBA), and related rules and regulations
- Accounting cost: this is the accrued cost determined by accounting rules (in accordance with a given accounting framework) and recognized and reported in general purpose financial statements (ultimately split between capital expenditures and operating expenditures)

London Hydro suggest that the current method using IFRS accounting has not been demonstrated to be deficient therefore should be kept as the method used.

d) Should the method for recovering costs relating to registered pension plans be different from that used for unregistered pension plans and OPEB plans?

London Hydro speaks only to OMERs which is a registered pension plan.

6. a) Should the OEB take into account impacts on financial reporting (US GAAP, ASPE and IFRS), legal, and tax matters?

London Hydro does note that using IFRS utilities can likely experience large year-to-year swings due to actuarial volatility, whereas a US GAAP utility would see that volatility smoothed out. London Hydro may suggest that in using IFRS for regulatory purposes it be allowed to modify IFRS to include a variance account to deal with the actuarial volatility.

b) If so, what are the issues that should be considered when determining the appropriate approach?

London Hydro suggests that there are issues with any form of financial reporting methodology with respect to OPEB and in adopting IFRS financial reporting as the standard utilities should be allowed to use a modified IFRS which includes a variance account for actuarial volatility.

c) For comparative analysis, how should the OEB address differences that arise from (driven by) the basis of accounting that is used by a rate-regulated utility? For example, the treatment of re-measurements under IFRS is different to their treatment under US GAAP and ASPE.

London Hydro suggests that the treatment of re-measurements under IFRS is different to their treatment under US GAAP. As noted above a variance account for actuarial volatility will help address some differences.

7. a) Would it be appropriate to establish a deferral or variance account(s) in association with the approaches discussed above in numbers 5) and 6) respectively?

As London Hydro noted above a variance account for actuarial volatility is recommended under modified IFRS.

Also as identified by London Hydro in our General Principles submission, opportunities for cost containment of legacy cost could be ignored by utilities because of inherent regulatory road blocks. Ignoring these opportunities may result in higher costs to customers in the long run. A variance account may be needed in certain situations to take advantage of opportunities. As discussed in our application to the OEB there are a number of approaches by which LDCs can satisfy their OPEB obligations. Many of these approaches are available to any business that is a going concern. The OEB should allow an LDC to seize opportunities when they present themselves. London Hydro believes it would be preferable to avoiding opportunities and incurring higher cost in the future. Establishing a deferral and variance accounts needed to address opportunities could be beneficial to all concerned. Obviously, it is incumbent on the utility to prove prudence before recovery.

b) How should the account(s) operate?

London Hydro understands that variance accounts for actuarial volatility are already are in use by some LDCs. Therefore methodology has been established.

With respect to an opportunities variance/deferral account this was discussed in our OEB application EB-2014-0196.

c) Should interest be applied to the account(s), and if so, why?

London Hydro suggests that there is no need to charge interest on the variance account for actuarial volatility.

With respect to an opportunities variance/deferral account interest application would be determinant by actions taken.

d) How should the transition from the current practice to the new method of recovery be addressed?

i. Should the transition be phased-in, applied retrospectively with catch-up adjustments for prior periods, prospectively with no adjustments for prior periods or a combination of any of these methods?

London Hydro would suggest the OEB allow LDCs to maintain their current methodology, pending a review at their next COS application, and as a result should be on a case-by-case basis.

ii. Should a generic approach be used or should the transition be addressed on a case-by-case basis?

London Hydro would suggest that it be on a case-by-case basis.

8. a) Would it be appropriate to establish some form of segregated fund or similar set-aside mechanism for amounts which are collected from ratepayers before they are paid out?

London Hydro does not believe that the OEB needs to direct establishment of some form of segregated fund or similar set-aside mechanism for amounts which are collected from ratepayers before they are paid out. London Hydro considers itself and operates accordingly as a going concern and perpetual entity. There should be no expectation that a well-managed utility would require a segregated fund.

b) What tax, legal, accounting or other issues arise?

London Hydro believes that there are tax implications for segregated fund or similar set-aside mechanism such as an irrevocable trust. This approach would require additional accounting and administrative costs as well.

c) How should the transition to the new practice be addressed?

i. Should the transition be phased-in, applied retrospectively with catch-up adjustments for amounts collected from ratepayers to date but not yet paid out, prospectively with no adjustments for prior periods or a combination of any of these methods?

London Hydro does not support establishing a segregated fund or similar set-aside mechanism, such as an irrevocable trust, as there has not been any demonstrated need or issues of sustainability that require a change in current practices.

ii. Should a generic approach be used or should the transition be addressed on a case-by-case basis?

London Hydro does not support establishing a segregated fund or similar set-aside mechanism, such as an irrevocable trust, as there has not been any demonstrated need or issues of sustainability that require a change in current practices.

9. What information should the utilities report and how frequently should it be reported?

London Hydro believes the OEB's current requirements supporting the methodology for municipally based electricity distributors with respect to pensions and OPEB's is sufficiently supported by the CoS application process. This is achieved through formulaic calculations for OMERs and actuarial valuation for OPEBs.

London Hydro OPEB Recovery History

Prior to year ended December 31, 1999

OPEB was treated on cash basis CICA 3460

January 1, 2000 CICA 3461 adopted by London Hydro

Opening OPEB Accrual funded through draw from Retained Earnings

May 1, 2002 De-regulation Opening rates based on Historical Test year ended December 31, 1999

OPEB was treated on cash basis CICA 3460

No OPEB accrual expense included in Historical year ended December 31, 1999

No OPEB expense recovered in Rates

May 1, 2006 First COS rates based on Historical Test year ended December 31, 2004

2004 OPEB annual expense included in rates

May 1, 2009 COS rates based on Forward Test year ended December 31, 2009

2009 OPEB expense forecast included in rates

May 1, 2013 COS rates based on Forward Test year ended December 31, 2013

2013 OPEB expense forecast included in rates