EB-2014-0099

Ontario Energy Board

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, (Schedule B);

AND IN THE MATTER OF an application by North Bay Hydro Distribution Limited for an Order or Orders approving or fixing just and reasonable rates and other charges for electricity distribution to be effective May 1, 2015.

WORKING CAPITAL ALLOWANCE SUBMISSIONS OF ENERGY PROBE RESEARCH FOUNDATION ("ENERGY PROBE")

September 11, 2015

NORTH BAY HYDRO DISTRIBUTION LIMITED
2015 RATES REBASING CASE

EB-2014-0099

SUBMISSION OF ENERGY PROBE RESEARCH FOUNDATION ON WORKING CAPITAL ALLOWANCE

A- INTRODUCTION

North Bay Hydro Distribution Ltd. ("NBHDL") filed a cost of service application with the Ontario Energy Board (the OEB) on December 12, 2015 under section 78 of the *Ontario Energy Board Act, 1998,* S.O. 1998, c. 15, (Schedule B), seeking approval for changes to the rates that North Bay Hydro charges for electricity distribution, to be effective May 1, 2015.

Procedural Order No. 1 was issued on March 19, 2015 which, among other things, provided for a Settlement Conference.

On May 19 and 20, 2015, all parties settled on all issues except for the working capital allowance ("WCA"). On July 16, 2015, the OEB issued its Decision and Order accepting the settlement proposal and approved the rates flowing from the settlement proposal on an interim basis pending the review of a lead-lag study that North Bay Hydro was to undertake.

On July 28, 2015, North Bay Hydro filed a study "Working Capital Requirements of North Bay Hydro Distribution Ltd.'s Distribution Business" ("Study") in response to the OEB's Decision and Order, July 16, 2015

This is the Submission of the Energy Probe Research Foundation ("Energy Probe") related to the WCA.

B - SUBMISSIONS

The Ontario Energy Board ("OEB") updated its policy with respect to the calculation of the allowance for working capital for electricity rate applications by way of a letter titled "Allowance for Working Capital for Electricity Distribution Rate Applications" dated June 3, 2015 ("Board Letter").

As part of the policy update, the Board reduced the default WCA percentage from 13% to 7.5%. As was the case in the past, distributors were given the option to request approval of a distributor-specific working capital allowance supported by appropriate evidence from a lead-lag study or equivalent analysis.

The Board further noted that the adoption of the new default value of 7.5% reflected not only the range of inputs that distributors had reported to the OEB, and that the adoption of this new default value reflected ***"a goal that <u>all distributors strive for best practices</u> in their administrative processes while supporting a distributor's basic cash flow requirements."*** (emphasis added)

Energy Probe has reviewed the Study filed by Navigant on behalf of NBHDL and has a number of submissions on the various components of the study that result in the requested WCA percentage of 10.43%. These submissions have been split between revenue lags and expense leads. Where Energy Probe has no issues or concerns with a particular lag and its derivation, no submissions have been made as those aspects of the WCA study have been accepted as filed.

I) REVENUE LAGS

a) Billing Lag

NBHDL is requesting a billing lag of 23.97 days. As shown in the response to Staff-2, this billing lag is well above the range of billing lags from other distributors that have filed lead-lag studies. In fact, the highest billing lag is 19.0 days, almost a full 5 days lower than that calculated and proposed by NBHDL.

Based on the response to Energy Probe-4 and Staff-2, this high billing lag appears to be the result of a unique billing process followed by NBHDL relative to other distributors.

NBHDL acquires meter data for the full calendar month on the last day of the month for the vast majority of its customers and then waits until the 15th of the following month for the net system load shape data it receives from the IESO in order to produce the bills. This means that all customers have to wait a minimum of 15 days for their bill to be issued.

NBHDL then takes up to the end of the following month (Staff-2) to produce all bills for customers where the meter data was taken from the end of the previous month. This means that customers will get their bills somewhere between 16 and 30 days after the meter data point.

Clearly this results in a significantly longer billing lag than is experienced by customers served by other distributors.

In addition, NBHDL has added 3 days to the billing lag to account for customers that receive their bill by mail (Energy Probe-1), as per the noted sections in the Distribution System Code. However, based on Appendix A in the Board Letter, the allowance for payments by mail is accounted for the collection lag, not in the billing lag.

Energy Probe submits that NBHDL is not following best practices in terms of getting their bills out to their customers in a timely manner consistent with other distributors. Energy Probe submits that the Board should reduce the billing lag from 23.97 days to 19.0 days, the highest billing lag seen by the Board to this date. This would provide an incentive to NBHDL to adopt best practices and reduce its cash flow requirements and at the same time reduce costs borne by ratepayers. It also reflects the movement of the days for mailing from the billing lag to the collection lag.

b) Collection Lag

NBHDL is requesting a collection lag of 24.56 days. The calculation of this figure is provided in the response to NBTA-2. Energy Probe submits that this analysis is flawed and should be rejected by the Board.

In particular, the first "bucket" used in the accounts receivable analysis is 0 to 30 days, which is longer than the amount of time customers have to pay and avoid late payment charges. This period is effectively 19 days for those customers that are mailed an invoice and 16 days for those customers that receive their bill electronically, as described in the response to Energy Probe-1, part (b).

In other words, it is unreasonable to assume that the accounts receivable in the first bucket (0 to 30 days) are received on average at 15 days. A review of the accounts receivable for distributors that have filed lead lag studies shows that the first bucket used by NBHDL is too large.

As an example, in EB-2014-0002, the study filed by Horizon Utilities had two buckets in place of the one used by NBHDL. The first bucket use by Horizon was 0 to 16 days and the second was less than 30 days. In the case of Horizon, more than 85% of the revenue in the first NBHDL bucket is in 0 to 16 day bucket. There is no reason to suggest that the figures would be significantly different for NBHDL, given that payment deadlines are the same for all distributors across the province

Given this flawed approach in using such a large first bucket, Energy Probe submits that the analysis provided by NBHDL is insufficient for the Board to rely on to set the collection lag.

Given the lack of reliable supporting evidence in this proceeding, Energy Probe submits that the collection lag should be set based on the policy as set out in the Board Letter. In particular, the Board set the default collection lag to 22.0 days to reflect the minimum payment period plus allowances for payments by mail as specified in s. 2.6 of the Distribution System Code. This is noted in Appendix A to the Board Letter.

c) Payment Processing Lag

NBHDL has proposed a payment processing lag of 1.80 days (pages8-9 of the Study). This figure was arrived at through the calculations shown in the table provided in the response to Energy Probe-1, part (g). As shown in the table and explained below it, NBHDL used a weighted average of the number of days to process payments based on a number of payment types to arrive at the weighted figure of 1.80%.

Energy Probe submits that there are two problems with the approach and numbers used by NBHDL.

First, NBHDL has used a figure of 4.21 days to process cash payments received in the office, excluding payments made by debit cards. This is because NBHDL has indicated that it only has two scheduled pick-ups by an armoured car service each week.

Energy Probe submits that the payment processing lag, as defined in the Study at page 8, is the time from *"when the customer provides a payment to NDHDL to such time as the funds associated with that payment are available to the company."* Energy Probe submits that the company has the funds available to it when it receives the cash, not when it transfers the cash to its financial institution. Furthermore, even if the payment is not considered available to NBHDL until the funds are transferred to the financial institution, NBHDL has not provided any evidence to support that any additional cost would be higher than the reduction in the WCA allowance built into the revenue requirement.

Second, and most importantly, the calculation shown in the response to the Energy Probe interrogatory results in a weighted average processing lag based on the number of payments, rather than on the dollar figures associated with the types of payments.

As explained in Appendix A to the Study, dollar weighting should be used for both leads and lags. An example is given under the heading of Dollar Weighting in the Study that illustrates the folly of using the number of transactions rather than the dollars associated with the transactions.

The example provided is equally applicable to the type of payments. Energy Probe submits it is extremely unlikely that the larger customers of NBHDL have an employee make a monthly trip to the NBHDL office with cash in hand to make their payments. Indeed it is reasonable to assume that the cash transactions are nearly all related to residential bills, which are, on average, significantly smaller than the bills paid by customers in other rate classes. Therefore, it is submitted that the evidence upon which the 1.80 days has been calculated does not stand up to scrutiny and should be rejected.

In its place, Energy Probe submits that the Board should use a payment processing lag of 1.40 days, which is the median used in the Board's letter. This would reflect that there is and should not be any significant variation between distributors for this activity.

d) Resulting Revenue Lag

The resulting revenue lag based on the proposed changes to the billing, collections and payment processing lags noted above are summarized in the following table, which is comparable to Table 4 in the Study.

Summary of Retail Revenue Lag

Description	Lag Days
Service Lag	15.25
Billing Lag	19.00
Collections Lag	22.00
Payment Processing Lag	1.40
Total	57.65

When this retail revenue lag is combined with the other revenue lag shown in Table 3 of the Study, the resulting weighted revenue lag is 57.73 days, a reduction of just under 8 days.

II) EXPENSE LEADS

a) PILs Expenses

Energy Probe submits that the PILs expense lead of (28.70) days as calculated in Table 15 in the Study is misleading and based on an abnormal payment schedule in 2014. As indicated in the response to Staff-7, *"Typically and in historic years, NBHDL has the installments, however in 2014 NBHDL fell behind in making the installments and decided to make a lump sum payment to catch-up"*.

As further indicated in the response to Staff-7 and found in Appendix C to the interrogatory responses, NBHDL's tax specialist provided the required federal tax installments for the following fiscal year (2014) as part of the 2013 tax return. This included the dollar amount required and the due date.

Energy Probe has calculated the expense lead for the PILs payments in the following table assuming NBHDL followed its usual practice and paid the installments on a monthly basis as indicated in the response to the interrogatory. For simplicity, Energy Probe has not assumed any payments for 2014 in January and February of 2015, given that the payments through to the end of 2014 would have been more than sufficient to meet the tax liability for 2014.

PILS Expense Recalculated

(based Appendix C to Staff-7)

Installment Payments	Weighting Factor	Payment Due Date	Service Lead Time	Payment Lead Time	Total Lead Time	Weighted Lead Time
44,146	0.066936661	31/01/2014	182.5	-334	-151.5	-10.14
44,146	0.066936661	28/02/2014	182.5	-306	-123.5	-8.27
57,123	0.086613123	31/03/2014	182.5	-275	-92.5	-8.01
57,123	0.086613123	30/04/2014	182.5	-245	-62.5	-5.41
57,123	0.086613123	31/05/2014	182.5	-214	-31.5	-2.73
57,123	0.086613123	30/06/2014	182.5	-184	-1.5	-0.13
57,123	0.086613123	31/07/2014	182.5	-153	29.5	2.56
57,123	0.086613123	31/08/2014	182.5	-122	60.5	5.24
57,123	0.086613123	30/09/2014	182.5	-92	90.5	7.84
57,123	0.086613123	31/10/2014	182.5	-61	121.5	10.52
57,123	0.086613123	30/11/2014	182.5	-31	151.5	13.12
57,120	0.086608574	31/12/2014	182.5	0	182.5	15.81
659,519	1	Total				20.39

This increases the PILs expense lead from (28.70) days to 20.39 days. Energy Probe submits that this figure of 20.39 days is more typical of NBHDL's payment of tax installments and should be used by the Board in the calculation of the overall WCA percentage.

b) Payroll Calculation in OM&A Expenses

NBHDL has proposed a payroll expense lead time of 9.36 days, as shown in Table 10 of the Study. However, as shown in the response to part (a) of Energy Probe-5, there are four anomalies in the calculation of this expense lead.

Virtually all of the payments made by NBHDL have an expense lead of 9 days, reflecting biweekly payments to its employees (14 days divided by 2), plus 2 days for the transfer of funds from NBHDL to its payroll administrator. There are also some line items that appear to reflect the payment of incentive amounts.

However, as shown in the table provided in response to part (a) of the interrogatory there are four line items that have negative expense leads. These are listed below.

Pay Period	Payment Date	Amount	Expense Lead Time	Weighting Factor	Weighted Expense Lead Time
17/03/2014 to 30/03/2014	3/4/2014	$ 82,926	(21.00)	3.40%	(0.71)
31/03/2014 to 13/04/2014	4/3/2014	$ 85,118	(5.00)	3.49%	(0.17)
07/08/2014 to 20/07/2014	7/24/2014	$ 93,742	(6.50)	3.84%	(0.25)
21/08/2014 to 03/08/2014	8/7/2014	$ 92,361	(6.50)	3.78%	(0.25)
					(1.38)

Unlike all the other payment dates shown, the first line item shown above, the payment date is actually before the pay period begins (March 3 as compared to the pay period of March 17 to March 30). Similarly the second line item shows a payment day of April 3, which is in the middle of the pay period of March 31 to April 13. Energy Probe submits that these payment dates are in error and the expense lead time should be changed from (21.00) and (5.00), respectively to 9.00 in both cases, consistent with other pay periods.

The third and fourth lines included in the above table appear to have errors in the pay periods. The third line shows a pay period that begins August 7, whereas it should be July 7 and the fourth line shows a pay period that begins August 21, where it should be July 21. This can be seen in a review of the pay periods around these two periods in the original interrogatory response. Again Energy Probe submits that these are errors in the calculation and the expense lead time should be changed from (6.50) to 9.00 in both cases.

The above changes would increase the expense lead from (1.38) for the four lines shown to 1.31 (being the sum of the weighting factors of 3.40%, 3.49%, 3.84% and 3.78% times 9.00 days), or an increase of 2.69 days.

This results in the expense lead calculated for payroll to increase from 9.36 days to 12.05 days. Replacing the 9.36 days in Table 10 with the corrected figure of 12.05 days would result in payroll & benefits weighted expense lead rising from 18.25 days to 19.59 days.

In turn this would increase the total OM&A expense lead shown in Table 9 from 15.28 days to 16.03 days. This figure would then be used in Table 17, as illustrated in the Summary of Recommendations below.

c) HST Calculation

The HST calculation shown in Table 16 of the Study contains an error in the calculation of the HST amount related to OM&A. The OM&A figure shown in Table 16 is $136,164. This is calculated as the total OM&A figure of $8,704,414 shown in Table 9 of the Study, times 13% (HST rate), times working capital factor shown in Table 16 of 12.03% (i.e. $8,704,414 x .13 x .1203 = $136,164).

As the Board is aware, HST is not paid on payroll & benefits or on property taxes. In other words, of the $8,704,414 of OM&A expenses shown in Table 9, only the miscellaneous OM&A figure of $3,763,376 is subject to HST. Making this change results in an HST figure of $58,855 ($3,763,376 x .13 x .1203) related to OM&A in place of the $136,164. This in turn reduces the $377,663 amount shown in Table 16 and used in Table 17 of the Study to $300,384.

III) SUMMARY OF RECOMMENDATIONS

Based on the above submissions, Energy Probe submits that the working capital allowance for NBHDL should be reduced to 7.97%. This figure is shown in the following table which is an update to Table 17 shown in the Study for each of the items discussed in the submission. The changes in the figures resulting from this submission are highlighted in bold.

Distribution Working Capital Requirements

	Revenue Lag days	Expense Lead Days	Net Lag Days	Working Capital Factor	Expenses	Working Capital Requirements
Cost of Power	**57.73**	33.02	24.71	6.77%	70,516,783	4,770,622
OM&A Expenses	**57.73**	**16.03**	41.70	11.42%	8,704,414	993,769
DRC	**57.73**	24.36	33.37	9.14%	1,778,578	162,495
PILS	**57.73**	**20.39**	37.34	10.22%	500,000	51,116
Interest Expense	**57.73**	44.80	12.93	3.54%	1,089,717	38,576
Total					82,589,492	6,016,578
HST						**300,384**
Total - Including HST						6,316,962
Working Capital as a Percent of OM&A incl. Cost of Power						7.97%

In summary, Energy Probe submits that the WCA should be reduced from the requested 10.43% to 7.97%.

In addition to reflecting the above noted changes, Energy Probe submits that the Board should direct NBHDL to have a third party conduct a study of best practices and costs and file this study as part of the next cost of service rebasing application. As noted in the above submissions, NBHDL has revenue related lags that are significantly higher than other distributors and expense leads that are shorter than other distributors.

This is the result of practices at NBHDL that appear to be significantly different from other distributors, resulting in higher cash flow related costs to NBHDL customers than to customers served by other distributors. As an example, as shown in the response to Staff-5 and Table 11 in the Study, NBHDL paid its property taxes earlier than required to both the City of North Bay and the Ministry of Finance. In the latter case, NBHDL paid the entire amount owing to the Ministry of Finance on April 3 whereas an interim payment was due on April 16 and a final payment was due on October 16. This clearly has a negative impact on cash flow that could easily be avoided.

As noted earlier in this submission, the Board's policy indicates that the default 7.5% reflects ***"a goal that all distributors strive for best practices in their administrative processes while supporting a distributor's basic cash flow requirements."***

As indicated in the response to Staff-2, NBHDL states that without a comprehensive cost-benefit analysis, NBHDL is not in a position to say if it would be able to reduce the billing lag, or what the additional cost to do so would be. Energy Probe agrees with NBHDL, and believes that a third party study of best practices and costs would be essential for such a cost-benefit analysis with respect to all facets of the lead-lag study.

C - COSTS

Energy Probe requests that it be awarded 100% of its reasonably incurred costs. Energy Probe worked with other intervenors in this proceeding to ensure complete coverage of the issues with a minimum of duplication. Energy Probe took the lead on the WCA issue.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

September 11, 2015

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