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BY EMAIL and RESS

September 23, 2015
Our File No. 20150003

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
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Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2015-0003 – PowerStream 2016-2020 – Threshold Scope Issue

We are counsel for the School Energy Coalition ("SEC"). Pursuant to *Procedural No. 3,* these are SEC's submissions on the threshold question: "what, if any, consideration should be given by the OEB to the announced merger between PowerStream, Enersource Hydro Mississauga Inc., Horizon Utilities Inc., and Hydro One Brampton Networks Inc., as part of its review of the application."[1] More specifically, is the "merger in scope or out of scope in this proceeding".[2]

Overview
SEC submits the merger is in scope in this proceeding, but that what consideration the Board should give to the merger impacts cannot be determined at this point, in absence of a full factual record.

Put another way, the question at this stage should not be how merger evidence should be applied, if it all, but only whether it should be considered. SEC submits the Board is required, in discharging its duty to set just and reasonable rates, to consider evidence relating to the impact of the proposed merger.

In considering this question, SEC disaggregates the Board's question into two components:

[1] *Procedural Order No. 3*, p.2
[2] *Ibid*

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- Should the Board have before it, in deciding rates that are proposed to be based on a forecast of future costs, all evidence potentially having material impacts on those future costs? Clearly the answer to this question, absent any extenuating circumstances, is yes.

- Should the Board apply its MAADs policy - i.e. to allocate the beneficial impacts of a merger to the shareholder in certain circumstances – to PowerStream? The answer to this question depends on the evidence before it. The Board cannot in law apply its MAADs policy until it considers whether, on the instant facts, it is appropriate. For that, the Board must look at the merger evidence.

Cost of Service Basis of Application

PowerStream's Custom IR application is based on an itemized forecast of its costs and revenues for each year of the proposed plan (2016-2020).[3] In response to interrogatories, PowerStream stated that the impact of the proposed merger has not been included in the Application.[4]

To determine just and reasonable rates, the Board at its core is determining what is a reasonable cost to serve PowerStream's customers. The evidence is that a merger is likely to occur, and that this may have a significant effect on that cost. PowerStream's rate plan is not derived from industry benchmarking or any other formula, but is based on PowerStream's forecast of costs and revenues for the test period.[5] The evidence is that the planned merger is likely to change the actual costs to serve PowerStream's customers during the test period. The forecasts in the Application are now not accurate, as they do not reflect what the actual forecast costs will be.

Publicly available information shows that PowerStream itself has told its shareholders that there will be material cost savings from the merger within the 5 year term of the Custom IR plan.[6] At the Technical Conference, while refusing to provide specifics, PowerStream admitted that the merger will likely lead to savings in capital and OM&A costs.[7] SEC has brought a motion to compel the production of certain merger documents, as the Board and parties require full information to do their job in setting just and reasonable rates.[8]

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[3] Section II, Ex. A, Tab 1, Schedule 1, p.1:

"PowerStream is proposing a five year Custom IR plan term, covering the 2016 to 2020 rate years, where the rates are determines in the following manner:

- The revenue requirement for each year of the five year IR term is determined based on the forecast rate base and costs;
- Inflation and productivity savings are incorporated in the capital and operating costs forecasts that underpin the revenue requirement calculation
- Customer counts and billing determinations are forecast for year; and"
- The Board's cost allocation methodology is applied for each year to ensure that the revenue requirement allocation to each customer class maintains the revenue to cost rations within the Board approved ranges."

[4] Interrogatory Response to I-Staff-1(a)

[5] Section II, Ex. A, Tab 1, Schedule 1, p.1

[6] 'PowerStream Merger and Acquisition, 'Briefing Document for the Vaughan City Council – Committee of the Whole (Working Session) Meeting September 22 2015, p.16, Figure 6 (Included as Appendix C to SEC"s Notice of Motion, filed September 18, 2015) https://www.vaughan.ca/council/minutes_agendas/AgendaItems/CW(WS)0922_15_1.pdf

[7] Technical Conference Transcript, p.55

[8] See Notice of Motion, filed by the School Energy Coalition on September 18, 2015

Merger Impacts Are A Forecast, Just Like All Other Costs

While no final merger agreement has been signed, the evidence is that this merger is more than likely to occur. PowerStream appears to believe so.[9] All that appears to be left is the final legal agreement.[10] Like any other aspect of a forward test year cost and revenue forecast, there are always unknowns and uncertainties. All the costs that PowerStream is seeking to recover in rates in this Application are forecasts – i.e. projections based on the best information it has at the time of filing.

Further, while there has to date been no MAADs approval of the merger, that in no way prohibits the Board from considering the impacts of one that is likely. The Board regularly considers cost impacts of activities that have not yet received all the necessary approvals. By way of example, new subdivisions that utilities forecast they will need to connect often have not have received requisite municipal approvals. Similarly, certain capital assets may still require environmental assessment approvals.

More specifically, as it relates to approvals that are required from the Board itself, it is not uncommon for utilities to include in their rate base costs that will require future leave to construct approvals, i.e. the utility cannot construct the asset without a separate approval from the Board. For example, in Union Gas' last cost of service application (EB-2012-0120) it included costs in the test year for the Owen Sound Replacement project[11] for which it later sought leave to construct approval.[12]

It is also not sufficient for PowerStream to rely on any MAADs application to deal with all merger related impacts. MAADs applications are not rate applications. It is <u>this</u> proceeding that is setting the rates for PowerStream's customers until 2020, not the MAADs application. The Board cannot defer consideration of relevant information that affects the underlying costs for which approval is being sought in this Application. A MAADs application is made pursuant to section 86, not the Board's rate-setting authority under section 78 of *the OEB Act*.

This is also not the first time the Board has had to deal with the convergence of a cost of service application and a MAADs application. This has already happened, in fact, to PowerStream.

In 2008, PowerStream filed its cost of service application for the 2009 rate year based on forecasts for PowerStream as a stand-alone utility. In the interim, it merged with Barrie Hydro,

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[9] For example, see the joint press release issued on September 15 2015, 'Local Electric Utilities Set to Approach Municipal Councils for Merger Approval' (Included as Appendix A to SEC"s Notice of Motion, filed September 18, 2015). Also PowerStream has set up a specific website to inform the public about the proposed merger. http://www.powerstream.ca/app/pages/MergerInfo.jsp

[10] Technical Conference Transcript, p.18-19:

> "MR. RUBENSTEIN: Well, let me unpack that. I recognize from there's no -- from what you are saying there is no final merger agreement, but is there a signed letter of intent, signed principles, that you will -- that you are going to translate into that document that -- and that's what you are working on?
> MR. MACDONALD: <u>Actually, I think we are past that. I think we really are trying to get all these agreements that are needed as part of a merger to get them finalized in the next number of literally couple of weeks, because we are trying to get it done by the end of September.</u>
> MR. RUBENSTEIN: So there is some document that exists that you have agreed to setting out some of the broad essences of the agreement that you haven't written into the final --
> MR. MACDONALD: That's correct." [emphasis added]

[11] EB-2011-0120, Ex. B1-5,p.5

[12] EB-2012-0430

and a MAADs application was brought. While the MAADs application was approved before the rates application truly got underway, the same issue arose about what to do with PowerStream's forecast budget, considering there was evidence of merger savings that would accrue.

In the PowerStream-Barrie MAADs decision, the Board made the approval conditional that the information on the merger could be used in the stand-alone PowerStream rates application.

> Notwithstanding our concern, the Board is prepared to approve the rate rebasing proposal advised by the applicants in this case provided it is understood that in the cost of service hearing parties will be free to introduce evidence that the costs, as filed, may not be the real costs and may not reflect actual costs. Parties may, in fact, take advantage of certain evidence introduced in this proceeding regarding cost reductions not revealed in the application as originally filed."[13]

The Board explicitly rejected the argument that the cost savings of the merger could not be considered in the context of the PowerStream cost of service application.[14]

While there was no specific issue in the approved issues list in the PowerStream 2009 rate case related to the merger, the preamble made clear that it was in-scope:

> It is understood that the cost and benefits attributable to PowerStream Inc. (For PowerStream ED-2004-0420 Rate Zone) related to the merger with Barrie Hydro Distribution Inc. are included in the scope of the specific issues listed below to the extent they relate to the 2009 test year. This includes allocation of share costs between PowerStream ED-2004-0420 and Barrie Hydro Distribution Inc. for the test year.[15]

In this case, there are a number of ways that the merger costs could have an impact on revenue requirement during the five year test period. Most obvious, the Board could decide that a lower cost forecast is appropriate, and so reduce rates over the period. Alternatively, the Board could decide that a five year cost of service approach is inappropriate, in light of the anticipated merger savings. That is, the Board could decide that the incremental rate increase sought, over and above fourth generation IRM, is unnecessary since the merger savings exceed the incremental increase.

Even if the Board ultimately determines that it should not give effect to the merger costs in setting PowerStream's rates, the information is still relevant to determining if the proposed Custom IR plan's 'annual adjustments'[16] or 'reopening and plan terminations'[17] are appropriate in any given year, either by way of baseline or by way of adjustments to the formula. This merger evidence may also have an impact on any earnings sharing and capital spending variance provisions, among other things.

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[13] EB-2008-0335, Transcript, Vol.1, p.198. Decision included at p.188-202.

[14] "We reject Mr. Vegh's notion that there is an implicit carve-out in this cost of service application, such that cost savings from mergers cannot be taken into account." (EB-2008-0335, Transcript, Vol.1, p.198)

[15] *Procedural Order No.2* (EB-2008-0244), Appendix B, Approved Issues List

[16] Section II, Ex. A, Tab 1, p.3

[17] Section II, Ex. A, Tab 1, p.5

MAADs Policy Does Not Make Merger Irrelevant

SEC also disagrees with any argument that the merger is not relevant because the *Report of the Board: Rate-making Association with Distributor Consolidation* ("MAADs Policy") allows emerging entities to keep any savings until the merged entity rebases, which can now be deferred for up to 10 years (previously 5).[18]

It is important to recognize that the MAADs policy is just that - a Board policy. It is not binding, and as a matter of law the Board cannot treat it as such without fettering its own discretion.[19] The Board must determine on the facts of each individual case whether the policy should be applied, or not.[20] In order to determine whether, and to the extent, it should apply the Board must have all the relevant information. That includes relevant information about the actual cost forecasts for the next five years, which includes the impacts of the merger. The Board cannot in law refuse to consider material information relevant to the application of the policy.

The Board may ultimately decide that it will not give effect to the merger cost savings in setting rates for PowerStream's customers, but it must consider that information. A decision that the cost savings should not be applied is not the same as a decision that the merger is out of scope in this proceeding.

Moreover, the appropriate application of the MAADs Policy to a situation such as this is far from clear. The policy does not speak directly to the present circumstances. In fact, the comments from the Board in the PowerStream-Barrie Hydro MAADs decision regarding the previous policy are applicable to the new one. In that decision, the Board was concerned that the policy appeared to assume that the consolidating entities that elected a deferral were under incentive regulation, not going in for cost of service.[21] It was in part for that reason that it added the condition discussed above. The same issues exist in the new MAADs policy, and will need to be resolved based on the facts of this case.

Conclusion

SEC submits the merger is clearly in scope in this proceeding. The evidence is clear that the merger will have an impact on the costs - and therefore rates - for PowerStream during the term

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[18] *Report of the Board: Rate-making Association with Distributor Consolidation* (EB-2014-0138), March 26 2015, p.6-7

[19] *Thamotharem v. Canada (Minister of Citizenship and Immigration)*, 2007 FCA 198, para 66:

> "Nonetheless while agencies may issue guidelines or policy statements to structure the exercise of statutory discretion in order to enhance consistency, administrative decision makers may not apply them as if they were law. Thus, a decision made solely by reference to the mandatory prescription of a guideline, despite a request to deviate from it in the light of the particular facts, may be set aside, on the grounds that the decision maker's exercise of discretion was unlawfully fettered: example, Maple Lodge Farms at 7. This level of compliance may only be achieved through the exercise of a statutory power to make "hard law", through, for example, regulations or statutory rules made in accordance with statutorily prescribed procedure." [emphasis added]

Without allowing parties to test and seek evidence from the utility that is in the general course relevant, it would be foreclosing before giving parties an opportunity to request the Board deviate from a policy in light of the particular facts.

[20] *Jackson v. Ontario (Minister of Natural Resources)*, 2009 ONCA 846, para 51:

> "Decision makers fetter their discretion when they fail to genuinely exercise discretionary power in an individual case, and instead automatically apply an existing policy or guideline: see David J. Mullan, Administrative Law (Toronto: Irwin Law 2001) at 115-116."

[21] EB-2008-0335, Transcript, Vol.1, p.197-8

of its plan. The Board must either give effect to those impacts, or not. In either case, it can only do so with all of the evidence before it relating to those impacts.

Yours very truly,
JAY SHEPHERD P. C.

Original signed by

Mark Rubenstein

cc: Wayne McNally, SEC (email)
Interested Parties (email)