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BY EMAIL

November 16, 2015

Kirsten Walli
Board Secretary and Manager
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: Horizon Utilities Corporation
Distribution Rate Application
Board File No. EB-2015-0075

Please find attached OEB staff's submission regarding Horizon Utilities Corporation's 2nd year update to its Custom Incentive Regulation application for 2015-2019.

Yours truly,

Original signed by

Jane Scott, Project Advisor
Ontario Energy Board

Attachment

2015-2019 Custom Incentive Regulation Rate Application – 2nd Year Update

Horizon Utilities Corporation

EB-2015-0075

OEB STAFF SUBMISSION

November 16, 2015

INTRODUCTION

On August 12, 2015, Horizon Utilities Corporation (Horizon) filed an application for its annual update to its 2015-2019 Custom Incentive Regulation (IR) application (EB-2014-0002) seeking an order approving just and reasonable rates and other charges for electricity distribution to be effective January 1, 2016. On August 27, 2015 Horizon filed an amendment to its application correcting Appendix C to the application and on November 5, 2015 Horizon revised its application by withdrawing the request for a deferral account for the implementation of monthly billing.

Procedural Order (PO) No. 1, issued October 7, 2015 and PO No. 2, issued October 22, 2015 approved the following intervenors who participated in a non-transcribed technical conference held on October 23, 2015:

Association of Major Power Consumers in Ontario (AMPCO)
Building Owners and Managers Association (BOMA)
City of Hamilton (City)
Consumers Council of Canada (CCC)
Energy Probe Research Foundation (EP)
School Energy Coalition (SEC)
Vulnerable Energy Consumers Coalition (VECC)

Horizon's 2015-2019 Custom IR (CIR) application resulted in a settlement proposal for all but issues pertaining to Cost Allocation and Rate Design. The settlement proposal was accepted by the Ontario Energy Board (OEB) on October 10, 2014 and the remaining issues were decided in the Decision and Order issued on December 11, 2014. The accepted settlement proposal established the framework for Horizon's CIR application. The requested updates for 2016 as set out in this application are a result of the settlement proposal and the Decision. The change in the base revenue requirement from the settlement proposal due to the adjustments is $0.113M, from $119.07M to $119.183M[1], or 0.1%. OEB staff supports Horizon's application with the exception of four issues:

[1] EB-2015-0075, Response to Undertaking JTC 3(a), Table 1, November 6, 2015

the proposal to update the Cost of Power for the Ontario Electricity Support Program charge, the proposal to update the street lighting load profile, the request to move the revenue-to-cost ratio for the street lighting class to 100% and the request to preapprove the cost allocation model for 2017-2019.

OEB staff sets out its submission with respect to the individual aspects of the application including off-ramps, re-openers, annual adjustments, disposition of Group 1 deferral and variance accounts and the update to the street light profile.

1. Off-ramps

Horizon's accepted CIR framework included the OEB policy of initiating a regulatory review if a distributor's annual performance was outside of the ±300 basis points or if performance erodes to unacceptable levels, would apply. Horizon does not yet have a full year's data and indicated that in its next annual update it would provide information on its 2015 performance. OEB staff supports this proposal.

2. Reopeners

Horizon's accepted CIR framework included a list of reopeners during the Custom IR period. This included changes to income tax rates and laws, changes to Ontario Market Rules or OEB Codes, changes to environmental laws that would impact business requirements and processes resulting in increased expenditures, changes to technical requirements beyond the control of the utility, items that would meet the OEB's Z-factor criteria, accounting framework changes that have a significant impact on the recording of expenses and revenues, and changes to amend distributor licences to allow market rates to be charged for wireless pole attachments. Horizon has indicated in its application that none of these reopeners is applicable for this second year update and OEB staff concurs.

In addition, the accepted CIR framework included the following reopeners, which are applicable to this update: changes to OEB policies on distributor rate design (*Report of the Board: A New Distribution Rate Design for Residential Electricity Customers* (EB-2012-0410), issued April 2, 2015), Ministerial Directives or similar required government action to provide a service to customers (implementation of the Ontario Energy Support Program (OESP) on January 1, 2016) and changes to the revenue allocated to unmetered load customers resulting from changes to the OEB's policies on cost allocation for unmetered loads (Cost Allocation Policy for Street Lighting, issued June 12, 2015).

a) Residential Distribution Rate Design

Horizon has proposed to move to fully fixed residential rates over a four year period. The evidence indicates that the annual increase in the fixed charge is $2.47[2] and for the 10th percentile (221 kWh) the impact associated with all changes in the cost of distribution service, including the adjusted rate design, is 4.95%[3]. Horizon has correctly implemented the OEB's direction on moving to a fully fixed residential distribution rate over four years. OEB staff concurs with Horizon's claim that mitigation is not required based on the conditions identified in the supporting filing requirements regarding the transition to fixed rates.

b) Ontario Electricity Support Program

Horizon has stated that the Cost of Power used for the Working Capital Allowance (WCA) calculation has not been updated to include the Ontario Electricity Support Program (OESP) commencing January 1, 2016. Horizon stated that it is awaiting the OEB's Decision on the final volumetric rate for the OESP and then it will update the cost of power, the revenue requirement and Tariff of Rates and Charges as part of preparing its draft Rate Order. OEB staff notes that Horizon has estimated the impact of this update as an increase in revenue requirement of $61,000[4] which is well below Horizon's materiality level of $0.3M from the 2015 CIR application[5]. OEB staff does not support the updating of the Cost of Power for the OESP at this time due to the nonmateriality and the uncertainty with respect to the net impact of the OESP on a utility's lead/lag calculations.

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[2] EB-2015-0075, Response to JTC 3(a), November 6, 2015
[3] *ibid*
[4] EB-2015-0075, Response to JTC 1, November 6, 2015
[5] EB-2014-0002, Exhibit 1, Tab 6, Schedule 1, p. 6, April 16, 2014

c) Cost Allocation for Street Lights

On June 12, 2015, the OEB issued a letter entitled *Issuance of New Cost Allocation Policy for Street Lighting Rate Class* (OEB New S/L Policy) requiring utilities to update the cost allocation model using a street lighting adjustment factor (SLAF) for the allocation of primary and line transformer assets and related costs rather than the existing allocation which is based on the number of street lighting connections.

Horizon has correctly calculated the SLAF as per the OEB's policy. As a result of this change, the revenue-to-cost ratio of the street light class increases to 170%. Horizon has proposed reducing this revenue-to-cost ratio to 100% resulting in a reallocation of $0.952M[6] from the street light class to other classes. OEB staff notes that OEB New S/L Policy allows for a revenue-to-cost ratio for the street lighting class of 80%-120%. The OEB adopted the range approach to revenue-to-cost ratios due to the level of uncertainty in the data used in the cost allocation models and required that distributors move the revenue-to cost ratio for each class within the range but noted that "as a practical matter there may be little difference between a revenue-to-cost ratio of near one and the theoretical ideal of one."[7] While the OEB has acknowledged that there is now greater certainty and understanding with respect to the costs associated with serving the street lighting class relative to past allocations[8], no additional evidence has been provided by Horizon that would justify moving to a revenue-to-cost ratio of 100% at this time; therefore OEB staff would recommend that Horizon reduce the street lighting ratio from 170% to 120% in 2016. This would result in a shift of $0.594M[9] from street lighting to the other classes. The move from 120% to 100% could be phased in over subsequent years in conjunction with other updates, if supported by further data.

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[6] EB-2015-0075, Response to JTC 9(a), November 6, 2015

[7] EB-20107-0667, Report of the Board, Application of Cost Allocation for Electricity Distributors, November 28, 2007, p. 7

[8] EB-2012-0383, Issuance of New Cost Allocation Policy for Street Lighting Rae Class, June 12, 2015, p.3

[9] EB-2015-0075, Response to JTC 9(a), November 6, 2015

Horizon provided cost allocation models for 2017-2019 in addition to 2016, and requested that the following be approved for 2017-2019:

- Implementation of the SLAF;
- Use of the OEB's version 3.3 cost allocation model;
- Street lighting demand and consumption updated for revised City of Hamilton Street Lighting Demand of 59,684kW per year, as entered on tab "I6.1 Revenue" in the Cost Allocation models;
- Street lighting demand allocators updated for revised City of Hamilton Street lighting demand of 59,684kW per year, as entered on tab "I8 Demand Data" in the cost allocation models; and
- 2016 distribution rates, updated for revised City of Hamilton street lighting demand 59,684kW per year, to be used as the starting point for rate design for 2017-2019.[10]

OEB staff submits that Horizon's SLAF and the use of OEB's version 3.3 cost allocation model could be approved for 2017-2019, subject to any future revised OEB cost allocation policies or models which the OEB determines should be implemented by utilities during a Custom IR period. However, the updating of the street lighting demand for the City of Hamilton should not be approved as explained in item 5 below.

3. Annual Adjustments

Horizon has made the following adjustments as per the accepted CIR framework:

a) Changes in the Cost of Capital

Horizon has correctly updated the cost of capital parameters in the response to Undertaking JTC3, using the 2016 Cost of Capital parameters issued by the OEB on October 15, 2015. In addition, Horizon has updated the stranded meters rate rider with the updated cost of capital parameters, as per the accepted CIR framework.[11]

[10] EB-2015-0075, Response to JTC 16, November 6, 2015
[11] EB-2015-0075, Response to JTC 10, November 6, 2015

b) Changes to Working Capital Allowance

Horizon has updated the following inputs to its working capital allowance:

i) Retail Transmission Service Rates have been updated to incorporate 2014 demand and 2015 Hydro One Uniform Transmission Rates.

ii) The Smart Metering Entity Charge has been updated to incorporate 2014 Residential and GS < 50 kW customer count.

iii) In its response to Undertaking JTC1, Horizon has updated the cost of power for the November 1, 2015 RPP prices.

iv) Horizon also updated the ratio of RPP vs. non-RPP volumes for 2014 actuals. In response to Undertaking JTC 2, Horizon provided its reference for making this adjustment, namely the response to Interrogatory 2-EP-9(b) in EB-2014-0002, which formed part of the settlement proposal.

c) Changes in tax rates

No adjustments were made due to changes in tax rates.

d) Changes in other third party pass through charges

Except for the third party pass through charges used in the calculation of the cost of power for the working capital allowance (part b) above), no changes have been made to third party pass through charges.

e) Earnings-Sharing Mechanism

The accepted CIR framework provided for a deferral account for earnings in excess of the OEB's annual approved regulatory return on equity (ROE). As the 2015 ROE is not available, the earnings sharing mechanism is not applicable to this annual filing. Horizon should report on the balance of the deferral account based on 2015 results in its 2017 annual update.

f) Capital Investment Variance Account

The accepted CIR framework provided for a deferral account to refund to ratepayers any difference in the revenue requirement if capital additions are lower than or the pacing of capital additions is slower than forecast over the 2015-2019 period. As the final 2015 capital additions is not available, the earnings sharing mechanism is not applicable to this annual update.

g) Efficiency Adjustment

The accepted CIR framework included an efficiency adjustment which would apply in the event that Horizon was placed in a less efficient cohort than the Cohort III which is Horizon's starting point. The *Board's Empirical Research in Support of Incentive Rate-Setting: 2014 Benchmarking Update for determination of Stretch Factor Assignments for 2016,* issue July 30, 2015 placed Horizon in Cohort III. As a result, no efficiency adjustment was made to the revenue requirement for the 2016 rate year.

4. Disposition of Group 1 Deferral and Variance Accounts

Horizon's 2014 actual year-end total balance for Group 1 accounts including interest projected to December 31, 2015 is a debit balance of $9,527,458 ($6,997,092 for Global Adjustment, $2,530,366 for the remainder). Horizon has requested approval for disposition over a one year period. The balance of the Group 1 accounts exceeds the disposition threshold of $0.001/kWh and are the same as the amounts reported as part of the OEB's *Reporting and Record-Keeping Requirements.*

Horizon has correctly calculated separate rate riders to recover the balances from Wholesale Market Participants, Regulated Price Plan (RPP) and non RPP customers as appropriate. In its response to Undertaking JTC11, Horizon clarified that the 2016 Global Adjustment Rate Rider will apply to all non RPP customers except Class A customers as of December 31, 2014, since Horizon's settlement process with these large customers does not result in a variance.

5. Update to Street lighting load profile

In conjunction with implementing the OEB's updated policy on cost allocation for street lighting, Horizon has proposed changing the load profile for the street lighting based on the reduced demand as a result of the City of Hamilton's conversion to light emitting diode (LED) lights. The change in the load profile of this one class shifts an additional $0.176M from street lighting to the other classes. Horizon explained "that it was appropriate to adjust the profile at this time because the Board had specifically revised its policies related to this particular class"[12]. OEB staff does not support this proposal. As the Board stated in the Decision for Horizon's Custom IR, in response to Horizon's request to update just the Large Users' load profiles for purposes of cost allocation; "Updated current hourly use information data for the large use class should not be used. Until more accurate data is available for all classes Horizon must continue to use the existing load profiles for the purpose of its forecast"[13]. OEB staff submits that the OEB's finding also applies to Horizon's request to update only the street lighting load profile as part of the 2016 update and therefore should not be approved.

All of which is respectfully submitted

[12] EB-2015-0075, Response to OEB Staff TC Question 14, October 23, 2015
[13] EB-2014-0002, Decision and Order, December 11, 2014, p. 6