



Ontario Energy Board Commission de l'énergie de l'Ontario

DECISION AND RATE ORDER

EB-2015-0065

ENERSOURCE HYDRO MISSISSAUGA INC.

Application for an order approving just and reasonable rates and other charges for electricity distribution to be effective January 1, 2016

BEFORE: Allison Duff
Presiding Member

Victoria Christie
Member

Cathy Spoel
Member

April 7, 2016

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1 INTRODUCTION AND SUMMARY

Enersource Hydro Mississauga Inc. (Enersource) serves about 202,000 mostly residential and commercial electricity customers in the City of Mississauga. As a licenced and rate-regulated distributor in Ontario, the company must receive approval from the Ontario Energy Board (OEB) for the rates it charges to distribute electricity to its customers.

Enersource filed an application with the OEB seeking approval for changes to its distribution rates to be effective January 1, 2016. The application contained a request for new distribution rates based on the Price Cap incentive rate-setting (Price Cap IR) option, Renewable Energy Generation (REG) funding and an Incremental Capital Module (ICM). The OEB issued a Partial Decision and Order on March 3, 2016 and Interim Rate Order on March 17, 2016 which addressed the Price Cap IR and REG requests.

This is the OEB's Decision and Order with respect to Enersource's request for an ICM.

An ICM is a means by which a distributor can receive additional revenue from customers to fund capital expenditures in the years between cost of service applications. Enersource sought ICM funding for \$68.3M, resulting in an additional 2016 revenue requirement of \$5.3M to be recovered through rate riders effective January 1, 2016¹. The ICM request included a payment to Hydro One Networks Inc. (Hydro One) and forecast 2016 capital expenditures.

After submissions from parties were filed, Enersource applied to the OEB for approval to defer its scheduled 2017 rebasing of distribution rates. The OEB approved Enersource's request. The deferral of Enersource's next cost of service application has affected the OEB's findings with respect to the ICM request. For the reasons outlined in this Decision, the OEB approves only ICM funding related to the Hydro One payment.

The total bill impact arising from this Decision for Enersource results in a monthly increase of \$0.68 or 0.46% for a residential customer consuming 800 kWh. When combined with the previous partial decision and order issued on March 3, 2016, the bill impact is a monthly increase of \$0.90 or 0.61%.

¹ As updated in EB-2015-0065, Undertaking JT1.17, January 18, 2016

2 THE PROCESS

Enersource filed its application on August 17, 2015. The OEB considered the application incomplete and requested additional information relating to the ICM request. After additional information was provided, the application was determined to be complete on October 2, 2015.

The OEB followed a standard, streamlined process for Enersource's Price Cap IR application. The OEB issued a Partial Decision and Order on March 3, 2016 approving all aspects of the application except the ICM request.

For the ICM component of the application, the following parties were approved as intervenors:

- The Association of Major Power Consumers in Ontario (AMPCO)
- Consumers Council of Canada (CCC)
- Energy Probe Research Foundation (Energy Probe)
- School Energy Coalition (SEC)
- Vulnerable Energy Consumers Coalition (VECC)

OEB staff also participated in the proceeding.

The OEB provided parties the opportunity to ask Enersource questions regarding its ICM request in writing through interrogatories and in person at a technical conference on January 8, 2016. Enersource subsequently filed a number of undertakings on January 18, 2016, updating its ICM request. The OEB decided to proceed with a written hearing, and received written submissions. The application, evidence and written submissions are on the OEB's website www.ontarioenergyboard.ca under file number EB-2015-0065.

3 INCREMENTAL CAPITAL MODULE

3.1 ICM Criteria

An ICM is available to distributors during the Price Cap IR years for capital investment needs that are additional to those approved through the last cost of service application.

Capital projects included in an ICM request must meet three criteria²:

- Materiality – each incremental capital project or expenditure must be material and clearly have a significant influence on the operation of the distributor
- Need – distributor must pass the Means Test; amounts must be based on discrete projects and directly related to the claimed driver, and must be clearly outside of the base upon which the rates were derived
- Prudence – amounts to be incurred must be prudent

In addition to the criterion that each project included in the ICM request be material, the total ICM request must exceed the ICM materiality threshold as described in section 3.5 below.

3.2 Project Materiality

Each capital project approved for ICM funding must be material to the distributor. Project materiality is 0.5% of distribution revenue requirement for distributors with a revenue requirement greater than \$10 million and less than or equal to \$200 million³. Enersource's last approved distribution revenue requirement was \$118M⁴ resulting in a project materiality of \$590,000.

3.3 Need and The Means Test

As part of the "Need" criterion, the OEB applies the Means Test when reviewing ICM applications. The Means Test states that if a distributor's regulated return exceeds 300 basis points above the deemed regulatory return on equity (ROE) embedded in its rates, the funding for any incremental capital project will not be allowed. Enersource

² Filing Requirements for Electricity Distribution Rate Application, Chapter 3 Incentive Rate-Setting Applications, July 16, 2015, p. 17

³ OEB's Report on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, July 14, 2008, section 2.6

⁴ EB-2012-0033

submitted evidence to show that its 2014 achieved regulatory ROE was 9.43% compared to the deemed ROE from the most recent cost of service application of 8.93%⁵, a difference of 50 basis points.

3.4 Prudence

To be eligible for ICM funding, expenditures must be prudent, illustrating good judgement in the management of capital budgets. Enersource's ICM request includes the actual Hydro One payment and the forecast capital expenditures for 2016. While the Hydro One payment is for a past expenditure based on studies and planning exercises, the forecasted expenditures in the capital budget are based on asset condition assessments and a draft Distribution System Plan.

3.5 ICM Materiality Threshold

The OEB expects a distributor to fund its capital expenditures within the ICM materiality threshold, before being eligible to apply for ICM funding. The ICM materiality threshold is deducted from the total ICM request to determine the amount eligible to be recovered from customers.

The OEB defined the ICM materiality threshold in Chapter 3 of the Filing Requirements for Electricity Distribution Rate Applications⁶ (the Filing Requirements). It represents a distributor's financial capacities underpinned by existing rates, including growth and a 20% dead band. The equation used to calculate the materiality threshold at the time of Enersource's application was as follows:

$$\text{Materiality Threshold Value} = 1 + (\text{RB}/\text{d}) * (\text{g} + \text{PCI} * (1 + \text{g})) + 20\%$$

Where:

RB = rate base included in base rates (\$)

d = depreciation expense included in base rates (\$)

g = distribution revenue change from load growth (%)

PCI = price cap index

Enersource calculated its materiality threshold value to be 164%, which is multiplied by the last approved annual depreciation of \$28.7M⁷ to determine the ICM threshold of \$47.2M.

⁵ Response to AMPCO-17, December 9, 2015

⁶ Filing Requirements for Electricity Distribution Rate Application, Chapter 3 Incentive Rate-Setting Applications, July 16, 2015, p. 17

⁷ EB-2012-0033

4 CAPITAL EXPENDITURES

Enersource forecast its 2016 capital expenditures to be \$46.2M in its 2013 cost of service application.⁸ Enersource updated its forecast for 2016 capital expenditures in this proceeding to \$115.1M. The following table provides historical information and compares the 2016 capital expenditure forecasts.

Table 1 – Annual Capital Expenditures

| \$000 | 2012 Forecast | 2012 Actual | 2013 Forecast | 2013 Actual | 2014 Forecast | 2014 Actual | 2015 Forecast | 2015 Updated Forecast | 2016 Forecast | 2016 Updated Forecast |
|------------------------------|------------------|----------------|------------------|----------------|------------------|----------------|------------------|-----------------------------|------------------|-----------------------------|
| System Service | 9,312 | 9,860 | 11,134 | 10,712 | 10,329 | 11,228 | 10,507 | 16,267 | 10,686 | 19,226 |
| System Renewal | 14,483 | 16,225 | 16,326 | 20,887 | 18,329 | 31,257 | 19,319 | 35,204 | 20,939 | 34,961 |
| System Access | 10,675 | 11,493 | 5,525 | 10,055 | 5,968 | 9,474 | 5,293 | 14,633 | 5,268 | 7,451 |
| General Plant | 29,472 | 29,220 | 13,187 | 6,831 | 10,725 | 6,231 | 9,646 | 10,585 | 9,317 | 12,935 |
| CAPITAL BUDGET | 63,942 | 66,798 | 46,172 | 48,485 | 45,351 | 58,190 | 44,765 | 76,689 | 46,210 | 74,573 |
| Hydro One TS payment | | | | | | | | | | 40,479 |
| TOTAL CAPITAL EXPEDITURES | | | | | | | | | | 115,052 |

Source: Undertaking JT 1.2

Enersource's ICM funding request was \$68.3M, equal to a 2016 total capital expenditure forecast of \$115.4M (including Allowance for Funds Used During Construction) less the ICM materiality threshold of \$47.2M.

The total capital expenditures of \$115.4M, was the sum of two distinct components in the capital plan. The first was to recover the cost of a payment to Hydro One of \$40.5 million relating to the construction of Churchill Meadows Transformer Station (Churchill Meadows TS). The second related to a 2016 forecast capital budget of \$74.6M.

⁸ EB-2012-0033, Exhibit 2, Tab 2, Schedule 2, Appendix 1, Table 17.6

4.1 Forecast Capital Expenditures Budget

In support of the 2016 forecast capital budget of \$74.6M, Enersource referred to an Asset Condition Assessment Study (Asset Study) performed by a third party in 2014, information not available at the time of the last cost of service. Enersource developed upgrade, rebuild and renewal plans, based on the new asset age and condition information, which resulted in a higher capital expenditure forecast for 2016.

Enersource filed a copy of the Asset Study and a draft Distribution System Plan for 2016-2021⁹ (DSP) in response to interrogatories. Enersource explained that the DSP was a draft because it did not reflect customer preferences¹⁰ and that it would file a final DSP with its next cost of service application.

Findings

The OEB does not approve ICM funding for the 2016 forecast capital expenditures budget request as it does not meet the ICM criteria. The OEB does not have the context required to approve a 2016 capital expenditure budget that is 60% higher than the forecast from Enersource's last cost of service. The OEB will not decide the ICM funding request based on an Asset Study alone given the deferral of Enersource's 2017 cost of service application.

Chapter 5 of the Filing Requirements instructs distributors to file a DSP when filing a cost of service application for the rebasing of their rates and provides that the OEB may also require a DSP to be filed in relation to an ICM¹¹. The OEB finds that the lack of a final DSP has impeded the assessment of the need and prudence for a request as sizable as Enersource's.

The OEB requires Enersource to file a final DSP before the OEB will consider ICM funding based on a 2016 forecast capital expenditures budget of \$74.6M. The Asset Study shows that many upgrade, rebuild and renewal plans extend beyond 2016. A five-year DSP will enable the OEB to consider the longer-term implications of Enersource's capital plans.

⁹ Attachment to Interrogatory Supp-Staff-15, December 9, 2015

¹⁰ EB-2015-0065, Supplementary ICM Evidence Summary, October 7, 2015, p.7

¹¹ Chapter 5: Consolidated Distribution System Plan Filing Requirements, March 28, 2013, p.7

The Filing Requirements for a DSP include the following items:

- the forecast impact of system investment on system O&M costs, including the direction and timing of the expected impacts¹²
- the activities undertaken to understand customer preferences (e.g., data access and visibility, participating in distributed generation, and load management) and how those preferences have been addressed¹³
- opportunities for continuous improvement in productivity, cost performance while delivering on explicitly stated reliability and quality objectives¹⁴

4.2 Payment to Hydro One

In 2005, Enersource participated with Hydro One and other utilities in a joint planning study¹⁵ to identify the need for transmission capacity in the Greater Toronto Area for the subsequent ten years. The forecast for Enersource's 44kV sub-transmission system anticipated annual load growth of 1.5%, and identified demand exceeding installed load-meeting capability at Erindale and Meadowvale transformer stations in 2006.

That study included a recommendation for the construction of a 230/44 kV transformer station (Churchill Meadows TS) in the vicinity of Winston Churchill Blvd. and Highway 403 within Enersource's service territory to relieve loading on Meadowvale TS and Erindale TS. The Churchill Meadows TS went into service in 2010. Enersource's load demand from Hydro One's 44 kV system, did not materialize as forecast.

The Transmission System Code (TSC) sets out cost responsibility principles for construction or modification of transmission facilities¹⁶. It states that load customers shall contribute capital to a transmitter to cover the cost of a facility required to meet their needs where the cost of the facility is not recoverable through revenues. The TSC also requires a transmitter to carry out a true-up calculation, based on actual customer load, for low risk projects, every five years¹⁷. This ensures that the customer – rather than the transmitter – bears the risk of the investment. This is also set out in the Connection and Cost Recovery Agreement between the transmitter and the distributor.

¹² *Ibid* p.19

¹³ *Ibid* p.4

¹⁴ *Ibid* p.5

¹⁵ GTA West Supply Study, Adequacy of Transmission Facilities and Transmission Supply Plan 2005-2015, February 16, 2006

¹⁶ TSC, Section 6.3.1

¹⁷ TSC, Section 6.5.3

In this case, Enersource is Hydro One's customer. Based on a forecast of incremental load growth on its whole 44kV system, Enersource paid a capital contribution to Hydro One of \$2.4 million in 2010.

When Hydro One conducted its fifth year review in 2015, none of the forecasted incremental load had materialized, so a true-up payment was required. Enersource made a \$40.5M payment to Hydro One on December 15, 2015 and has included that payment in the 2016 ICM request.

The intervenors submitted that the OEB should not approve the ICM funding request related to the payment to Hydro One as it was made in 2015 and should be considered out-of-period for a 2016 ICM request. SEC stated in its submission that "[the] Applicant is asking the Board to change the ICM policy so they can claim an ICM for an out-of-period expenditure."¹⁸ Energy Probe submitted that OEB approval of this request would "open to all distributors to come and seek an ICM based on not only forecasted capital expenditures in the subject year but also on actual capital expenditures in a previous year..."¹⁹.

Enersource submitted that when it filed the ICM application, it expected a payment date in 2016, not 2015.²⁰ Enersource submitted that the payment met the ICM criteria of need, materiality and prudence. OEB staff submitted that Enersource was not in control of the payment date and that the payment met the ICM criteria and should be approved as requested²¹.

Findings

The OEB approves the ICM request related to the \$40.5M payment to Hydro One. The payment is distinct from the budgeted capital expenditures included in the ICM request.

The Uniform System of Accounts requires a paid capital contribution to be classified as an intangible asset and depreciated over time²². The Churchill Meadows TS will be classified in this way and the payment made to Hydro One will be added to rate base when Enersource next rebases. The question is whether rate relief, through an ICM

¹⁸ EB-2015-0065, SEC Final Argument, February 3, 2016, p.3

¹⁹ EB-2015-0065, Energy Probe Submissions, February 2, 2016, p.4

²⁰ Connection and Cost Recovery Agreement

²¹ EB-2015-0065, OEB Staff Submission, February 2, 2016, p.8

²² Uniform System of Accounts, Section 1609 Capital Contributions Paid

rate rider, should be approved until Enersource's rates are rebased. The OEB finds that rate relief is appropriate.

The OEB will not make a finding as to whether or not Enersource knew it would have to make the payment in 2015. The evidence indicates that Enersource filed the ICM application in 2015 before the payment amount and date were set. The OEB finds the 16-day period between the December 15, 2015 payment date and January 1, 2016 fiscal year start, an insufficient basis on which to disqualify or disallow the ICM funding request.

The Hydro One payment meets the three ICM criteria. The payment exceeds the project materiality criteria of \$590,000 and relates to a discrete project, outside the base upon which rates in 2013 were derived. The decision to build the Churchill Meadows TS resulted from a need identified in the regional planning study and the subsequent payment to Hydro One was contractually required. The OEB finds that Enersource meets the Means Test as its 2014 actual regulatory ROE was 9.43%, within 300 basis points of the deemed regulatory ROE of 8.93%. In addition, the amount was prudently incurred as the payment accorded to the methodology and inputs prescribed in the OEB's Transmission System Code.

The \$40.5M payment does not exceed the ICM materiality threshold of \$47.2M. While the OEB has considered the Hydro One payment as distinct from the other budgeted capital expenditures, it is clear that Enersource is forecasting spending up to \$74.6M on other capital expenditures in 2016. While Enersource may choose to delay some of these forecast expenditures in the absence of approval of the ICM relating to them, the evidence also indicates that Enersource's annual capital expenditures have exceeded \$40M since 2012. Given the circumstances of this ICM request, the OEB finds it reasonable to assume Enersource's 2016 capital expenditures will meet the ICM materiality threshold (if the Hydro One payment is included), given its historical annual capital spending.

The OEB finds that the \$40.5M Hydro One payment meets all the OEB's ICM criteria.

The OEB directs Enersource to recover from Hydro One and return directly to the Enersource customers, any portion of the \$40.5M payment associated with a materialization of the proposed 44kV load in the future. This will be determined in the calculation made every five years, the next one being in 2020.

5 IMPLEMENTATION

When Enersource was planning to rebase in 2017, it proposed to apply the half-year rule to calculate the revenue requirement for the ICM request²³. As the OEB approved Enersource's request to defer its 2017 rebasing²⁴, the full \$40.5 capital expenditure, the annual depreciation rate and return must be included in its ICM revenue requirement calculation.

The OEB approves the proposed 40-year amortization period for determining the annual depreciation rate.

The ICM rate riders will be effective and implemented on May 1, 2016. The OEB does not approve Enersource's proposal for a January 1, 2016 effective date. The OEB finds that Enersource did not file a complete application until October 2, 2015, which did not allow sufficient time to complete this proceeding prior to January 1, 2016. As a result, Enersource will not collect the forgone revenue for the first 4 months of 2016. The OEB estimates the forgone revenue to be \$1M, which will not be recovered from customers in 2016 or in a future period when Enersource rebases.

The ICM revenue requirement has been assigned to customer rate classes in the same proportion as the OEB-approved distribution revenue from the OEB's last cost of service decision. In accordance with the OEB's rate design policy, the rate rider to recover the ICM revenue requirement for residential customers has been calculated as a fixed monthly charge. For all other classes, the rate riders have been calculated using the fixed/variable split from the last cost of service decision.

The OEB has revised the ICM model in order to calculate the rate riders to be implemented as a result of this Decision. A copy of the model is attached.

The ICM rate riders will be effective until Enersource's next cost of service rate order. At that time, Enersource will include this asset in its rate base. Consistent with the policy to update the useful lives of its assets upon rebasing, the OEB observes that Enersource may wish to revisit the amortization of the intangible asset to more closely align with the service life of the Churchill Meadows TS.

²³ EB-2014-0219, Report of the Board: New Policy Options for the Funding of Capital Investments: Supplementary Report, January 22, 2016, 8

²⁴ OEB Letter to Enersource, March 22, 2016

As the payment amount is a known, actual number, the OEB does not find it necessary to order Enersource to track collected revenues from the ICM rate riders for the purpose of a possible adjustment.

As the OEB has approved the ICM rate riders in this rate order, Enersource's 2016 rates will no longer be interim.

6 ORDER

THE ONTARIO ENERGY BOARD ORDERS THAT:

1. The Tariff of Rates and Charges set out in Schedule A of this Order will become final effective May 1, 2016, and will apply to electricity consumed or estimated to have been consumed on or after May 1, 2016. Enersource Hydro Mississauga Inc. shall notify its customers of the rate changes no later than the delivery of the first bill reflecting new rates.
2. Enersource Hydro Mississauga Inc. will ensure that any credit that results from future reconciliations under the Connection and Cost Recovery Agreement with Hydro One is returned to Enersource Hydro Mississauga Inc.'s customers.
3. The intervenors shall submit their cost claims no later than 7 days from the date of issuance of this Decision and Rate Order.
4. Enersource Hydro Mississauga Inc. shall file with the OEB and forward to the intervenors any objections to the claimed costs within 17 days from the date of issuance of this Decision and Rate Order.
5. The intervenors shall file with the OEB and forward to Enersource Hydro Mississauga Inc. any responses to any objections for cost claims within 24 days from the date of issuance of this Decision and Rate Order.
6. Enersource Hydro Mississauga Inc. 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 number, EB-2015-0065 and be made electronically through the OEB's web portal at <https://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 <http://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.

With respect to distribution lists for all electronic correspondence and materials related to this proceeding, parties must include the Case Manager, Jane Scott at Jane.Scott@ontarioenergyboard.ca and OEB Counsel, at Richard.Lanni@ontarioenergyboard.ca.

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DATED at Toronto, **April 7, 2016**

ONTARIO ENERGY BOARD

Original Signed By

Kirsten Walli
Board Secretary

SCHEDULE A
DECISION AND RATE ORDER
ENERSOURCE HYDRO MISSISSAUGA INC.
EB-2015-0065
TARIFF OF RATES AND CHARGES
APRIL 7, 2016