September 22, 2016

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St., Suite 2700
Toronto, ON, M4P 1E4

via RESS and Courier

Dear Ms. Walli:

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

The Coalition of Large Distributors ("CLD") consists of Enersource Hydro Mississauga Inc., Horizon Utilities Corporation, Hydro Ottawa Limited, PowerStream Inc., Toronto Hydro-Electric System Limited, and Veridian Connections Inc.

Consultation Overview

On May 14, 2015, the Ontario Energy Board ("OEB") notified stakeholders that it was initiating a consultation on rate-regulated utility pensions and other post-employment benefits ("OPEBs") in the electricity and natural gas sectors. The consultation process began with an invitation to stakeholders to provide submissions on an initial set of questions. Accordingly, on July 31, 2015, the CLD filed its comments with the OEB.

On May 19, 2016, the OEB advised that it had retained KPMG to prepare a report to assist the OEB in understanding the issues and options that may be available. The OEB convened a Stakeholder Forum (the "Forum") for July 19 and 20, 2016 to discuss the issues in this consultation. The Forum consisted of: i) an introduction and overview of pension and OPEB accounting and the methods presently used by Ontario's regulated utilities; ii) a presentation of the KPMG report, with an opportunity for participants to ask questions of KPMG; and iii) stakeholder presentations, with an opportunity for other participants to ask questions of the presenters.

In a letter dated June 23, 2016, the OEB informed stakeholders that it will accept submissions on this consultation by September 22, 2016. On August 10, 2016 the OEB informed stakeholders that it would benefit from submissions on two objectives identified in the KPMG Report: i) principles that the OEB should adopt for purposes of assessing pension and OPEB costs in rate applications, including any principles the OEB should adopt in considering the appropriate rate mechanisms for cost recovery; and ii) options for rate mechanisms for cost recovery. The OEB stated in the letter that it is particularly interested in parties' views on whether a set-aside mechanism is necessary for OPEBs if accrual accounting values should be used for rate setting, and on the latter two options put forward by KPMG (reduction to rate base and a tracking account).

The OEB also requested parties' views on whether either of these two mechanisms could be implemented for pension costs, in the event that the OEB favours using accrual accounting values for rate setting. The OEB also requested parties' views on KPMG's modified funding contribution method, as well as any method other than a pure accrual accounting method as the basis for cost recovery.

The CLD is pleased to offer the following submission on these matters in this consultation. The CLD's submission focuses on OPEB costs and will not address issues related to pension costs. All CLD members and indeed most distribution companies in Ontario, are members of the Ontario Municipal Employees Retirement System ("OMERS"). At the Forum, there was general agreement that the current accounting treatment of OMERS costs was fair to both the ratepayers and distributors. As a result, no change to the current method of including these costs in rates is expected nor recommended.

Principles that the OEB should adopt for purposes of assessing OPEB costs in rate applications, including any principles the OEB should adopt in considering the appropriate rate mechanisms for cost recovery

The CLD continues to support the five principles offered in its presentation:

i. basic principles of rate setting and accounting
ii. intergenerational equity/fairness
iii. cost stability
iv. cost efficiency
v. proportionality

The application of basic principles of rate setting and accounting is generic but worthy of inclusion, as it was in the *Report of the Board: Transition to International Financial Reporting Standards* ("IFRS Report"). In the IFRS Report, the OEB found general agreement on these principles and, in the CLD's opinion, nothing that occurred during the discussion at the Stakeholder Forum would contravene their inclusion in this proceeding either.

Further in the IFRS Report, examples of what was meant by "basic principles" included, "fairness, minimizing intergenerational inequity and minimizing rate volatility." The CLD submits that its proposed principles of intergenerational equity/fairness, cost stability and cost efficiency are in strong alignment. The distinction we draw between cost efficiency and proportionality is that the former addresses matters of an absolute nature (e.g., the amount of administrative effort required to implement a given approach), while the latter is intended to capture relative considerations (e.g., how much administrative effort is required by other costs of a similar magnitude).

On their merits, the CLD believes that due consideration to these principles will guide the OEB towards a decision in the public interest and an outcome that is consistent with the Renewed Regulatory Framework for Electricity Distributors ("RRFE") objectives.

The CLD continues to support accrual accounting for OPEBs. The CLD respectfully submits that the OEB look specifically to the principles of intergenerational equity and cost stability for guidance. From Toronto Hydro's initial submission, "intergenerational equity provides that ratepayers in a given period should pay only the costs necessary to provide them with service in that period." This consideration tips the scales heavily in favour of the accrual accounting method

for OPEBs "because it results in the recovery of… OPEB costs in the same period in which employees provide the services [from which current ratepayers benefit]." This method reflects utilities' true cost of doing business. Moreover, the CLD submits that the pay-as-you-go method of accounting would be more volatile for ratepayers and utilities alike because it is more sensitive to the cumulative health status of retirees in a given year.

A change to the existing methods could result in significant effort and cost to determine adjustments necessary to true-up existing methods to a new way of cost recovery. These adjustments would require significant oversight and testing by the OEB and intervenors to ensure all parties are treated fairly. A change to a new method would introduce the potential for added volatility and uncertainty in rates. As KPMG stated on page 5 of its introduction presentation provided at the Stakeholder Forum on July 19, 2016:

> *"There is no guarantee that one method (accrual accounting versus cash payments) will always result in higher (or lower) costs for a given period than the other… Despite periodic differences in P&OPEB costs for the two methods, in the fullness of time, the cumulative cash (or funding) costs for a plan (or arrangement) is generally expected to equal that plan's cumulative accrual accounting costs (timing issue only)".*

Furthermore, the CLD continues to support a case-by-case approach for set-aside mechanisms. During the Forum, the differing circumstances among utilities that weigh on this consultation were identifies: varying OPEB frameworks, bargaining outcomes and financial reporting standards to name a few. It is unlikely that a single, cross-sector regulatory approach will result in an outcome that is cost efficient for all utilities.

Options for rate mechanisms for cost recovery

As noted above, the CLD continues to see benefit in the current method of accounting for OPEBs and supports the use of accrual accounting to recover these costs from rates. The transition to a new system of recovery could be punitive to distributors or to ratepayers without consideration given to what was included in rates in prior years. Typically, current OPEB plans provide a lower level of benefit and cost than the plans in place in prior years. In some cases, customers would have paid more through rates than amounts expended by the distributor in prior years where this will reverse in future years. To now implement a tracking system with a true-up in future rates to reconcile to a cash basis could result in customers paying a higher cost than if the existing methods were permitted to continue.

Is a set-aside mechanism necessary for OPEBs if accrual accounting values should be used for rate setting, and on the latter two options put forward by KPMG (reduction to rate base and a tracking account)

The CLD submits that a set aside mechanism is not necessary since differences between accrual and cash will balance over time. If the process changes part way through that period, it is possible for one of the parties to be negatively impacted.

However, should the OEB determine that a mechanism is necessary and differences between accrual accounting and cash payments are tracked in variance accounts, the CLD recommends that a tracking account be used to track differences between amounts recovered from customers and amounts paid for OPEBs. The CLD supports the use of interest rates to be used on these

balances at the same rate as any other deferral and variance account ("DVA") as indicated in Table 1 below. In May 2006, Board Staff conducted a review of the interest rates used for regulatory accounts and released a proposal paper for comment. In Board Staff's recommendation it stated that many utilities use internally generated funds as opposed to short term debt to finance these balances in regulatory accounts. Staff stated *"It can be debated that these internally used funds represent an opportunity cost to the LDC and in that case, it could be argued a forgone investment opportunity (e.g., T-bill or GICs)".* The Board determined that the three-month bankers' acceptance rate plus a static spread of 25 basis points would be used for regulatory accounts which supports the lost opportunity position. The CLD views these OPEB balances like any other regulatory account balance and supports the use of this rate since it most accurately incorporates any benefit or cost to the regulated entity or its customers.

The CLD does not support the use of a set aside mechanism for gains and losses on actuarial revaluations recorded in Other Comprehensive Income ("OCI"). However, these amounts could be tracked in variance accounts in the same manner as the above with an offset account. These are non-cash balances and as such should not incur carrying charges. Balances in the accounts would be reviewed at future rebasing applications and if material, distributors would have an opportunity to defend the disposition of these amounts. The following is a summary of the accounts and amounts that would be recorded in each account:

Table 1: Amounts Recorded in Deferral and Variance Accounts

	Cash payments less recoveries (Net of Tax)	Carrying Charges	Amounts recorded in OCI (Net of Tax)
CASH ITEMS			
Pensions			
Capital	XX	DVA Rate	
Offsetting Mirror Account	-XX	none	
OM&A	XX	DVA Rate	
Offsetting Mirror Account	-XX	none	
OPEBs			
Capital	XX	DVA Rate	
Offsetting Mirror Account	-XX	none	
OM&A	XX	DVA Rate	
Offsetting Mirror Account	-XX	none	
NON-CASH ITEMS			
Revaluation Gains and Losses			
Actuarial Gains and Losses		none	XX
Offsetting Mirror Account		none	-XX

Could either of these two mechanisms (reduction to rate base and a tracking account) be implemented for pension costs, in the event that the OEB favours using accrual accounting values for rate setting

As stated above, members of the CLD pay contributions to the OMERS pension plan and the current recovery of these costs is fair and appropriate. These costs are predictable and any variance between amounts recovered from rates and amounts paid would be immaterial.

Comments on KPMG's modified funding contribution method, as well as any method other than a pure accrual accounting method as the basis for cost recovery

The modified funding contribution method represents the minimum amount of contributions required to be made by a sponsor of a registered pension plan that is subject to the requirements of pension legislation under the Pension Benefits Act, Ontario, modified by the fact that only an employer's normal cost contribution and going concern special payments using the 15-year amortization period are included in the current period's rates. CLD members are members of the OMERS pension plan and accordingly would not recognize revaluation adjustments from a modified funding contribution method.

If you have any questions with respect to the above, please contact the undersigned.

Sincerely,

Original signed by Indy J. Butany-DeSouza

Indy J. Butany-DeSouza, MBA
Vice President, Regulatory Affairs
Horizon Utilities Corporation

Gia M. DeJulio
Enersource Hydro Mississauga Inc.
(905) 283-4098
gdejulio@enersource.com

Indy J. Butany-DeSouza
Horizon Utilities Corporation
(905) 317-4785
indy.butany@horizonutilties.com

Gregory Van Dusen
Hydro Ottawa Limited
613-738-5499 ext. 7472
regulatoryaffairs@hydroottawa.com

Colin Macdonald
PowerStream Inc.
(905) 532-4649
colin.macdonald@powerstream.ca

Andrew Sasso
Toronto Hydro-Electric System Limited
(416) 542-7834
asasso@torontohydro.com

George Armstrong
Veridian Connections Inc.
(905) 427-9870 x2202
garmstrong@veridian.on.ca