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BY E-MAIL

February 5, 2018

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

Dear Ms. Walli:

Re: Ontario Energy Board File Number: EB-2017-0269

Application for approval of share purchase, amalgamation and related matters – Newmarket-Tay Power Distribution Ltd. and Midland Power Utility Corporation

In accordance with Procedural Order No. 2, please find attached OEB Staff's Supplementary Interrogatories in the above proceeding. The attached document has been forwarded to the applicants and to all other registered parties to this proceeding.

Yours truly,

Original Signed By

Judith Fernandes
Project Advisor

Encl.

OEB Staff Supplementary Interrogatories

Newmarket-Tay Power Distribution Ltd.
Midland Power Utility Corporation

Application for approval of share purchase, amalgamation and related matters

EB-2017-0269

February 5, 2018

2-Staff-1
Ref: OEB Staff Interrogatory No. 4 and Section 6.16 of the Share Purchase Agreement

The applicants have confirmed that the legal name of the amalgamated entity will be Newmarket-Tay Power Distribution Ltd.

The applicants have also indicated that they intend to continue to use the Midland Power name and its related branding in Midland Power's current service territory for a period of ten years following the closing of the proposed transaction, including on customer bills or invoices as well as maintaining signage existing as at the closing date.

Assuming the proposed transaction and related approvals (cancellation of Midland Power's licence) are approved by the OEB:

a) Please explain why the applicants wish to continue to use the Midland Power name and related branding when Midland Power is no longer licensed by the OEB.

b) Please explain how the continued use of the Midland Power name and relating branding does not cause confusion for consumers and how applicants intend to inform consumers that the legal, licenced entity is no longer called “Midland Power”.

c) Please comment on the foregone synergies from not being able to consolidate billing, maintenance of signage, etc.

2-Staff-2
Ref: OEB Staff Interrogatory No. 5

In part 5 a) of the response, the applicants have provided a calculation relating to the expected increase to rates for Midland Power's commercial customers. There is presently a consultation underway regarding rate design for Commercial and Industrial customers.

a) Please explain Newmarket-Tay's approach to rate design for Midland Power's commercial and industrial customers if the OEB establishes a new Commercial and Industrial rate policy before the end of the ten-year deferred rate rebasing period.

In the response provided to 5 b), the applicants state: "The migration of MPUC and Tay service areas to a direct connection to the IESO grid is also expected to lower customers bill costs in relation to line losses."

Loss factors are only updated at the time of rebasing, which the applicants are proposing would only occur after 10 years, even if a direct connection to Hydro One's high voltage (Transmission) grid comes into service earlier. Customers would still be paying for losses based on current approved loss factors.

a) Please explain how customers will be benefiting from any lowered losses due to establishing a direct connection to the Hydro One high voltage transmission system prior to rebasing.

2-Staff-3
Ref: OEB Staff Interrogatories No. 6 and No. 8

In OEB Staff Interrogatory No. 6 the applicants have provided a revised Table 3, setting out transaction and transition costs for NT Power and Midland Power. The table lists NT Power's transaction costs as $1.2M in year 1.

In OEB Staff Interrogatory No. 6, the applicants set out Midland Power's transition costs over a 10-year period.

a) Please provide a cost breakdown of NT Power's transaction costs. Please confirm whether this includes the additional $200,000 that is being paid by NT Power for Midland Power's transaction costs and expenses.

b) Please provide a detailed explanation of what is incorporated in Midland Power's transition costs and please explain why these transition costs are increasing over the ten-year period.

In part b) of the response to OEB Staff Interrogatory No. 6, the applicants state that the difference in the stated synergies, between page 22 of the evidence and Table 3 in the pre-filed evidence is owing to the transition cost for annual rent of the 16984 Highway 12 property.

c) Please explain why the annual rent payable for this property is considered a transition cost rather than an operational cost when the response to OEB Staff Interrogatory No. 8 indicates that this property will be utilized going forward to consolidate all operational and administrative functions for the Tay and Midland areas.

2-Staff-4
Ref: OEB Staff Interrogatory No. 7

The applicants have shown cost savings/synergies for each year of the ten-year period in Table 3 in the pre-filed evidence and in response to OEB Staff Interrogatory No. 6. However, in the response provided to OEB Staff Interrogatory No. 7, the costs attributable to the specific business operations that make up the projected cost savings are only provided for year 10.

a) Please provide a breakdown of the projected cost savings by the specific business operations for each year, from year 1 to year 10 arising from this transaction.

The response reflects savings of $700,000 in management and staff costs in year 10. The response also states that the projected cost savings are assumed to occur through natural attrition through retirements and as employees leave.

b) Please explain the applicants' basis for the $700,000 projected cost savings in year 10.

The response indicates projected savings for facilities of $55,000.

c) Please explain what this represents.

d) Please provide the expected savings from the consolidation of the Tay and Midland areas.

2-Staff-5
Ref: OEB Staff Interrogatory No. 12

The response provided states that the portion of the $11.9M that is paid which is a premium and not recovered from the cost synergy savings in the first ten years will be fully recovered from the amalgamated entity's earnings from year 11, and specifically from the entity's return on equity.

a) Please explain what is meant by the applicants' proposal to recover the premium from the consolidated entity's return on equity from year 11.

b) Please explain whether such an approach is consistent with the OEB's expectation that the premium is fully recovered from efficiencies generated during the deferred rebasing period.

c) In light of the applicants' proposal to recover the balance of the premium from the amalgamated entity's return on equity, please comment on the impact this will have on financial viability.

d) Please explain how the applicants intend to track the recovery of the acquisition premium from year 1 onwards.

The applicants have provided a table which reflects the financial ratio projections of the combined utility.

e) For comparison purposes, please provide a similar table that shows the current financial ratios of the amalgamating utilities on a combined basis.

2- Staff-6
Ref: OEB Staff Interrogatory No. 15

The applicants have indicated that they are financing 90% of the proposed transaction with new term-debt from the bank.

a) Given the current trend of rising interest rates, please confirm whether the applicants have performed a sensitivity analysis to ensure that the financial viability of the combined utility would not be threatened if interest rates rise.

b) Please confirm if the financial projections and financial ratios for the combined entity includes the new term-debt financing of the proposed transaction.

c) If the projected financial ratios in b) do not include the new term-debt financing, please explain how the additional borrowing impacts the debt to equity ratio and the financial viability of the consolidated entity, in light of the premium being paid on this transaction.

2- Staff-7
Ref: SEC Interrogatory No. 8

The applicants have not answered this interrogatory, and have instead referred to OEB Staff Interrogatory No. 12 but that OEB Staff interrogatory does not provide the requested information. OEB staff believes that this information would be helpful in assessing the financial viability of the merged entity and requests that the applicants provide a response.

2- Staff-8
Ref: SEC Interrogatory No. 12

OEB staff requests a response to this interrogatory posed by SEC as the requested information would be helpful in assessing the impact on the financial viability of the merged entity.

2- Staff-9
Ref: SEC Interrogatory No. 14

In response to this question, the applicants have referred to SEC Interrogatory 12, which was not answered by the applicants.

The applicants have also referred to OEB Staff Interrogatories 16 and 17. OEB staff notes that those questions provide a very different context.

OEB staff requests that the applicants provide an answer to this question as it would be helpful in assessing the financial viability of the merged entity.

2- Staff-10
Ref: OEB Staff Interrogatory No. 18

In the response provided, the applicants have explained that the proposed Earnings Sharing Mechanism (ESM) would operate in such a way that excess earnings during years 6 through 10 would be recorded in a deferral and variance account (ESM account), with disposition to occur at the time of rebasing, i.e. in year 11. The applicants have proposed to first use any amounts in the ESM account for rate mitigation that might be required and, for any remaining balance to be distributed to all customers, “in a manner acceptable to the Board”. This differs from the ESM set out in the Handbook to Electricity Distributor and Transmitter Consolidations, which requires annual assessment of earnings and excess earnings to be shared with customers annually.

a) Under the applicants’ proposal, please confirm whether interest accrues to the balance of the ESM account. If so, please advise of the rate that the applicants are proposing would apply, and explain why. If no interest would apply, please explain your reasons.

b) If there are overearnings from years 6 to 10:

   i. Please confirm that it would be considered that all customers overpaid, absent detailed information that showed how specific customer classes over-contributed based on existing rates as adjusted over time.

   ii. Please explain why the applicants are proposing that any balance in the ESM account first be applied for any mitigation and why this would not constitute inter-class subsidization at the time of rebasing.

c) Please provide the applicants’ views on the proposed ESM disposition only at the time of rebasing which creates the potential for inter-generational inequity, in that customers at rebasing or for a period thereafter benefit from over-earnings realized during the period from years 6 to 10, which would otherwise be shared with minimal lag under the OEB’s policy for annual disposition of any ESM balance.

2- Staff-11
Ref: OEB Staff Interrogatory No. 24

In part b) of the response, the applicants state that the projections in the pro-forma statements are based on 2015 actual with cost and customer growth of 2.9% to 3.0% respectively.

a) Please explain how the projected customer growth of 3.0% is derived, providing information on the historical customer growth that would support the assumptions being made.

b) Please provide the projections in the pro-forma statements if customer growth is assumed to be 0%.

2- Staff-12
Ref: OEB Staff Interrogatory No. 25

In Interrogatory No. 25, OEB staff requested information on how it intends to communicate with customers regarding differences in specific service charges between the Newmarket-Tay and Midland rate zones. NT Power has responded stating that it intends to maintain separately branded websites to facilitate customer communication by service area.

a) Please explain how the maintenance of two separately branded websites will not cause confusion for customers, given the proposed amalgamation of the two distributors.

2- Staff-13
Ref: OEB Staff Interrogatory No. 26

The applicants have confirmed that Conditions of Service will be consolidated and harmonized at the time of rebasing, in year 11. While the Conditions of Service are required to be filed with the OEB, the OEB does not approve the Conditions of Service.

a) Please explain why the applicants are not considering efforts to review and consolidate and harmonize the Conditions of Service earlier than rebasing, identifying any barriers with respect to this matter.

2- Staff-14
Ref: SEC Interrogatory Nos. 15(d) and 20

NT Power has confirmed that it last filed a Distribution System Plan (DSP) in December 2015 and has indicated that the merged entity will file a DSP for the Midland Power rate zone after closing the transaction. NT Power is due to file its next DSP with the OEB by December 2020.

a) If the proposed amalgamation transaction is approved, please confirm that the applicants will be filing a DSP for the consolidated entity by December 2020. If not, please explain.