PUBLIC INTEREST ADVOCACY CENTRE
LE CENTRE POUR LA DÉFENSE DE L'INTÉRÊT PUBLIC

March 14, 2018

VIA E-MAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St.
Toronto, ON
M4P 1E4

Dear Ms. Walli:

Re: EB-2017-0045 Halton Hills Hydro Inc.
2018 IRM Electricity Rate Application
Vulnerable Energy Consumers Coalition (VECC) Submission

Attached please find VECC's final submission in the above proceeding. As per Procedural Order No. 3 we have also filed a copy with the Applicant as well as all Intervenors via email.

Yours truly,

Original signed

Ben Segel-Brown
Counsel for VECC

Cc: David Smelsky, Halton Hills Hydro Inc.
Intervenors

1204-ONE Nicholas Street, Ottawa, ON K1N 7B7 Tel: 613-562-4002 Fax: 613-562-4002 piac@piac.ca; www.piac.ca
Ben Segel-Brown Tel: 613-562-4002x29 bsegel-brown@piac.ca

EB-2017-0045

Halton Hills Hydro Inc.
Application for electricity distribution rates effective
May 1, 2018

VECC Submission
March 14, 2018

Halton Hills Hydro Inc. (HHHI) filed three applications with the Ontario Energy Board (OEB) on September 25, 2017, October 23, 2017 and December 1, 2017 for rates pursuant to the OEB's Price Cap IR framework, for the establishment and disposition of a variance account to account for and remedy an error related to depreciation expense, and for recovery of costs incurred as a result of a pay equity settlement agreement (Z factor), respectively.

The applications were filed under section 78 of the *Ontario Energy Board Act*, *1998*, S.O. 1998, c. 15, (Schedule B) and under the OEB's Filing Requirements for Incentive Regulation Rate Applications seeking approval for changes to HHHI's electricity distribution rates to be effective May 1, 2018. The OEB decided to hear the three applications as part of the same proceeding.

VECC was granted intervenor status regarding HHHI's Z-factor, and HHHI's application for the establishment and disposition of a variance account to account for and remedy an error related to depreciation expense.

A) Z-factor Application

HHHI's Z-factor application seeks recovery of $261,251 ($258,348 plus $2,902 in carrying costs) for operations, maintenance and administration (OM&A) costs including OMERS costs, related to pay equity adjustments based on the settlement agreement between HHHI and Power Workers Union (PWU), CUPE Local 1000.

The above amount includes pay equity payments for the period between January 1, 2012 to November 30, 2017 and projected incremental costs from December 1, 2017 to March 31, 2021. HHHI plans to true-up all projected costs at the time of final disposition. The total Z-factor amount is reduced to $259,764 when 2017 actuals are used.[1]

HHHI seeks approval of a fixed rate rider over a 36-month period effective period May 1, 2018 to April 30, 2021. HHHI has updated the rate riders for customer numbers at December 31, 2017, actual 2017 hours and adjusted carrying charges.[2]

The OEB's guidelines indicate Z-factors are subject to the three criteria of causation, materiality

[1] VECC IR#7
[2] Appendix IRR H

and prudence[3] and must satisfy all three.

As discussed below, VECC's position is that HHHI's Z-factor application for Pay-Equity adjustments does not meet the OEB's causation and materiality criteria.

Causation

Z-factors provide for unforeseen events outside the control of a distributor's ability to manage. The cost to a distributor of these events must be material and its cost causation clear.
The OEB expects that any application for a Z-factor will be accompanied by a clear demonstration that the management of the distributor could not have been able to plan and budget for the event and that the harm caused by extraordinary events is genuinely incremental to their experience or reasonable expectations.

Since 1988, HHHI has been working on pay equity as a routine, on-going business issue.[4] This is not a new practice. HHHI established a Pay Equity Committee[5] and in 1990 HHHI established a Pay Equity Plan. The driver for HHHI's Pay Equity Plan was the 1988 Pay Equity Act.

Periodic testing of Pay Equity is part of an employer's ongoing obligations and HHHI's Pay Equity Committee conducts ongoing reviews of its Pay Equity Plan. HHHI has had a previous material Pay-Equity adjustment pay-out. In 1990 HHHI reached a Pay-Equity resolution: $58,291.60 for union and $8,972.60 for management, and monies were paid out over a five-year period.[6] HHHI did not file a Z-factor application at that time.

HHHI's management are part of the Pay Equity Committee and compliance with the Pay Equity Act is expected. HHHI has the experience that the elimination of a single male comparator job class can lead to material changes in pay equity.[7] When this occurred in 2012[8] (removal of Custodian) and the pay review process began, HHHI would have been aware early on that this would lead to pay-outs as the male comparator for purposes of pay equity maintenance was removed. The review process spanned 5 years (2012 to 2017) and HHHI had input to the process and negotiated the outcome with PWU. In VECC's view, and the Pay-Equity adjustment was predictable and HHHI should be reasonably expected to plan and budget for such an occurrence. The 2014 letter[9] from the Premier to the Minister of Labour did not change the Pay-Equity landscape for employers. The letter asked the Minister to develop a wage gap strategy with the Minister Responsible for Women's Issues. The letter did not reference a strict, specific requirement for employers. HHHI's reliance on this Letter to justify its Z-factor adjustment is misplaced.

[3] Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors July 14, 2008
[4] Board Staff IR#9 (b)
[5] Board Staff IR#12
[6] VECC IR#3
[7] Board Staff IR#13 (a & b)
[8] Z-factor Application Page 5
[9] Appendix IRR G

Given that HHHI works on Pay-Equity as a routine business issue, VECC submits the Pay-Equity adjustment was not an unforeseen event outside the control of HHHI's ability to manage. VECC expects there have been many previous pay equity settlements in the gas and electricity sector which were not the subject of Z-factor applications. Pay equity settlements should be accepted as a business risk accounted for in the return on common equity.
Furthermore, VECC submits the retroactive pay equity adjustment is a result of systemic gender discrimination by management in compensation for work performed by employees in predominantly female job classes. If pay had been fairly allocated between male and female employee classes, no pay equity adjustment would have occurred. Because pay equity settlements arise from systemic gender discrimination which is within management's control, pay equity settlements are not eligible for Z-factor treatment. VECC notes that in the past the OEB has historically excluded from Z-factor treatment "litigation costs since these were, to a significant degree, under control of management and also related to the business risk of the Company, a factor in the determination of the allowed return on common equity."[10] As a matter of policy, the OEB should not insure regulated entities against litigation risks by allowing them to recover the costs of settlements from consumers. This will encourage regulated entities to comply with their legal obligations.

Materiality

The amounts must exceed the Board-defined materiality threshold and have a significant influence on the operation of the distributor; otherwise they should be expensed in the normal course and addressed through organizational productivity improvements.
For a distribution revenue requirement less than or equal to $10 million, the Board determined that a $50,000 materiality threshold applies. Based on a 2016 distribution revenue requirement[11] of $9,953,991 (net of revenue offsets), HHHI's materiality threshold is $50,000. The OEB's guidelines indicate the threshold must be met on an individual event basis in order to be eligible for potential recovery.
For every year of the Z-factor claim, the amount related to the pay equity adjustment for both salary and OMERs is well below HHHI's materiality threshold of $50,000.[12] The maximum amount of $27,353 (salary & OMERS) is in 2015. The minimum amount is $19,633 (salary & OMERS) in 2017. VECC submits that HHHI's proposed Z-factor does not satisfy the $50,000 Materiality criterion for each of the years 2012 to 2021 as the amounts for each year do not exceed the threshold.

Other Considerations

In HHHI's 2012 Cost of Service application (EB-2011-0271) the OEB approved OM&A spending on an envelope approach.[13] HHHI's annual Pay Equity costs between are manageable within this "envelope" of OM&A. For each of the years 2012 to 2014, HHHI's achieved ROE is above the amounts approved in rates.[14] Given the overearnings in these three years, incremental pay

[10] E.B.R.O. 497-01 at para 111, 212.
[11] EB-2015-0074
[12] VECC IR#7
[13] Board Staff IR#11
[14] Board Staff IR#11

equity expenses for these years should not be borne by ratepayers.
In VECC's view, HHHI had the ability to absorb the annual pay equity adjustments within its operating budget without having a materially adverse impact on its financial position or its ability to carry out its operations and business activities.

Prudence

The amount must have been prudently incurred. This means that the distributor's decision to incur the amount must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.

HHHI's Pay-Equity review process took five years concluding in February 2017. The process evaluated positions and came to an agreement on a Terms of Reference, eligible positions, position data collection, adjustment window and male comparators.[15] VECC submits the expenses was prudent.

The Pay-Equity agreement includes $35,957 for Pay Equity Advisory expenses.

In VECC's view the review process took an unreasonable amount of time and costs should have been flagged earlier. As part of HHHI's 2016 Cost of Service application, the Pay-Equity issue should have been identified and reviewed even if the full impact was not known at that time.

HHHI is applying for recovery of a Z-factor claim of $259,764 including carrying costs for Pay-Equity adjustments for the period January 1, 2012 to December 31, 2017 and projected incremental costs for the period January 1, 2018 to April 30, 2021.[16]

As discussed above, VECC's position is that HHHI's Z-factor claim does not meet the Board's criteria of causation and materiality and the Board should not approve HHHI's request. For similar reasons, VECC does not support HHHI's request to recover forecast costs for the years 2018 to 2021. The forecast annual amounts for 2018 to 2021 are below the materiality threshold and should be absorbed within HHHI's OM&A spending envelope.

Should the Board accept HHHI's Z-factor application, VECC makes the following comments on HHHI's proposal for 2018 to 2021. In response to SEC IR#10, HHHI indicates the approved Tariff of Rates in 2018 to 2021 would indicate a Rate Adder versus a Rate Rider. HHHI indicates the recovery in future years would be for advanced funding to mitigate or smooth the anticipated rate impact that would occur at the time of rebasing anticipated for May 21, 2021. HHHI expects that all costs would be trued-up at the time of rebasing. HHHI references Smart Meters as an example of where funding adders have been used.

VECC does not support HHHI's proposal for advance funding. Funding adders were approved as part of the Smart Meter roll-out as it was a government mandated program and advanced funding was needed for implementation. HHHI's Pay-Equity adjustments are not comparable to

[15] Z-factor Application Page 8
[16] Z-factor Application Page 8

Smart Meter implementation. Employers have an obligation to develop and maintain Pay Equity plans. Adherence is more a matter of ongoing review and negotiation, rather than a strict, specific requirement.[17] It is not appropriate for customers to pay in advance for Pay-Equity adjustments that are below the materiality threshold.

Notification

In addition to the 3 criteria of causation, the OEB's Z-factor Filing Guidelines also indicate a distributor must notify the OEB promptly by letter to the Board Secretary of all Z-factor events. Failure to notify the OEB within six months of the event may result in disallowance of the claim.

The pay equity adjustments were finalized in February 2017. HHHI filed a Notice of Intent to file a Z-factor application on June 29, 2017. This was the first time the Board was made aware of the Z-factor. HHHI did not signal a Z-factor application was on the horizon at the time of its 2016 Cost of Service application. HHHI did not file the Z-factor application as part of the 2018 IRM application filed on September 25, 2017. HHHI filed its Z-factor application on December 1, 2017.[18]

HHHI's Pay-Equity process began in 2012 and was completed in 2017.

Distributors are expected to report events to the OEB promptly and apply to the OEB for any amounts claimed under Z-factor treatment with the next rate application. This will permit the OEB and any affected distributor to address extraordinary events in a timely manner. Subsequently, the Board may review and prospectively adjust the amounts claimed under Z-factor treatment.

VECC submits HHHI fell short on the OEB's expectations to notify the OEB promptly of its Z-factor event and this should be taken into consideration in determining if the OEB will accept HHHI's claim.

Summary

A Z-factor adjustment is a mechanism to address unforeseen or extraordinary events outs ide of management's control.

For the reasons discussed above, VECC submits HHHI's Z-factor claim for Pay-Equity adjustments is not genuinely incremental to HHHI's experience or beyond the control of management, and it is not material in any given year.

VECC submits the OEB should not approve HHHI's Z-factor request.

B) Recovery of Depreciation Expenses

HHHI seeks approval for an accounting order to establish a new deferral and variance account (the Depreciation DVA) and the annual allocation of $330,259 to correct the calculation of depreciation amounts for the years 2016 to 2021. The Depreciation DVA is intended to account for and remedy an error in the calculation of the depreciation expense in HHHI's most recent

[17] VECC IR#3

[18] Board Staff IR#8 (a)

Cost of Service (COS) Application with rates effective May 1, 2016.[19] The estimated depreciation impact of $330,000 over the five years is approximately $1.6 million.[20]

In 2012, HHHI completed a review of the useful lives of its assets. HHHI extended the useful lives for several asset classes and the remaining useful lives for some assets had to be adjusted. In 2017, HHHI discovered it had understated the deprecation which results in an annual revenue deficiency of $330,259 beginning in 2016. HHHI indicates that the error is the result of an inadvertent mistake in Excel modelling and administrative in nature.[21]

Given that the 2016 depreciation amount was cleared on a final basis the Board must determine if any adjustment to 2016 depreciation violates the legal requirements concerning retroactive ratemaking.

HHHI's 2016 COS application was resolved by way of a Settlement Proposal with intervenors on all issues that was accepted by the OEB. VECC submits it is not appropriate for HHHI to make an adjustment to this Settlement Proposal now as the settlement reached was the result of negotiations on all issues including the depreciation expense and the impact of additional request of $330,259 may have impacted the outcome of the final settlement. HHHI did not communicate the error with the other signatories to the Settlement Proposal EB-2015-0074.[22] The onus is on HHHI to ensure the evidence it files in support of its application is complete and accurate as clearly stated in the 2016 Filing Requirements for Electricity Distributors. The Board has determined in previous decisions that utilities are entrusted by ratepayers to ensure its calculations are correct.[23] VECC submits HHHI did not meet its responsibility to do so.

The Settlement Agreement in EB-2015-0074 states "There are Appendices to this Settlement Proposal which provide further support for the proposed settlement. The Parties acknowledge that the Appendices were prepared by HHHI. While the Intervenors have reviewed the Appendices, the Intervenors are relying on the accuracy of the underlying evidence in entering into this Settlement Proposal.[24]

VECC notes HHHI had an issue in its 2012 COS application that resulted in an audit of Account 1575 that included a review of depreciation values. HHHI indicates it recognized the implications of its 2012 COS application and began a process to replace an aging ERP system that was not designed to calculate depreciation expenses under MIFRS. The new system was not fully implemented to provide the depreciation calculation for the 2016 COS and HHHI relied on Excel spreadsheets where the error occurred.[25] Further, the Chapter 2 Appendices alert applicants to specifically incorporate changes impacting remaining useful lives from adopting

[19] EB-2015-0074 for 2016 COS Application
[20] SEC IR#1
[21] Board Staff IR#15 (a)
[22] Board Staff IR# 15(c)
[23] EB-2017-0056 Kitchener-Waterloo Hydro Inc. Page 9
[24] EB-2015-0074 Page 3
[25] Board Staff IR#19 (a)

MIFRS in the calculation of depreciation values. HHHI indicates it was an oversight that it did not take action to capture the correct changes when calculating depreciation amounts due to these alerts. HHHI assumed it was not applicable since it had made the transition to MIFRS in the 2012 COS.[26] Given the issue in 2012 and the Chapter 2 alerts, VECC submits HHHI should have learned from its mistakes and the onus was on HHHI to provide more rigorous controls, review and diligence with respect to calculating accurate 2016 depreciation expenses.

VECC submits that to correct the balances now would be retroactive ratemaking. The account balances in 2016 were disposed of through final tariffs approved by the OEB. VECC submits the OEB should apply the principle of “no retroactive ratemaking” to prevent a retroactive adjustment.

ALL OF WHICH IS RESPECTFULLY SUBMITTED March 14, 2018.

[26] Board Staff IR#22 (a)