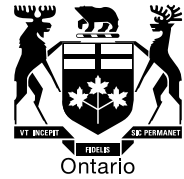


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**BY EMAIL**

February 21, 2019

Ms. Kirsten Walli  
Board Secretary  
Ontario Energy Board  
2300 Yonge Street, 27<sup>th</sup> Floor  
Toronto ON M4P 1E4

Dear Ms. Walli:

**Re: Algoma Power Inc. and Dubreuil Lumber Inc.  
Application for approval for Dubreuil Lumber Inc. to sell its distribution system to Algoma Power Inc.  
OEB Staff Submission**

**OEB File No. EB-2018-0271**

In accordance with Procedural Order No. 2, please find attached the OEB Staff Submission for the above proceeding. This document has been sent to Algoma Power Inc. and Dubreuil Lumber Inc.

Algoma Power Inc. and Dubreuil Lumber Inc. are reminded that their Reply Submissions, if any, are due by March 7, 2019.

Yours truly,

*Original Signed By*

Valerie Bennett  
Project Advisor, Application Policy and Climate Change

Encl.



## **OEB Staff Submission**

**Application for approval for Dubreuil Lumber Inc.  
to sell its distribution system to Algoma Power  
Inc.**

**Algoma Power Inc. and Dubreuil Lumber Inc.**

**EB-2018-0271**

**February 21, 2019**

# 1 INTRODUCTION AND OEB STAFF POSITION SUMMARY

## 1.1 Overview of the Application

Dubreuil Lumber Inc. (DLI) and Algoma Power Inc. (API) (collectively, the Applicants) filed an application (Application) on September 24, 2018 under Sections 74, 77, 78, and 86 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15 (Schedule B) (Act), for leave to sell DLI's distribution system to API, and for API to incorporate that system into its existing regulated distribution business. The Applicants requested the following approvals from the Ontario Energy Board (OEB):

- DLI's proposed sale of its electricity distribution system, substantially in its entirety, to API pursuant to Section 86(1)(a) of the Act
- Cancellation of DLI's Electricity Distribution Licence<sup>1</sup> pursuant to Section 77(5) of the Act
- Cancellation of API's Interim Distribution Licence<sup>2</sup> to operate DLI's distribution system pursuant to Section 77(5) of the Act
- Amendment of API's Electricity Distribution Licence<sup>3</sup> pursuant to Section 74(1) of the Act, by:
  - Adding the Township of Dubreuilville (Township) to the description of the service area in which API is authorized to distribute and sell electricity
  - Adding a condition to provide API with limited relief from regulatory liability for circumstances arising from its acquisition
- The partial disposition of the balance recorded in API's OEB-approved Interim Distribution Licence Deferral Account from DLI customers pursuant to Section 78(2) of the Act
- The establishment of a new deferral account to record transaction and integration costs incurred by API, for recovery from all API customers after the acquisition, in lieu of a deferred rate rebasing period, pursuant to Section 78(2) of the Act
- The classification of customers acquired by API in the DLI service area in accordance with API's existing rate classes upon the closing of the proposed transaction, after which they may be billed in accordance with API's approved Tariff of Rates and Charges
- The endorsement by the OEB of API's proposed approach to allocating costs attributable to the DLI service area to be used, at the time of API's next rebasing, primarily to API's R1 and R2 rate classes, which are eligible for Rural or Remote Electricity Rate Protection

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<sup>1</sup> ED-2012-0074

<sup>2</sup> ED-2017-0153

<sup>3</sup> ED-2009-0072

To enable the proposed transaction, on August 27, 2018, the Applicants entered into an Asset Purchase Agreement (APA). As part of the APA, API will purchase substantially all of the assets used in the operation of DLI's electricity distribution business<sup>4</sup> in the Township for the price of \$45,000 and assumption of liabilities. API is not seeking cost recovery for the purchase price.<sup>5</sup>

Based on the requests in the Application, this submission has been divided into two parts. The first contains OEB staff's submissions on matters associated with the mergers, acquisitions, amalgamations and divestitures (MAADs) elements of the Application; and the second pertains to rates-related matters. As highlighted in the *Handbook to Electricity Distributor and Transmitter Consolidations* (MAADs Handbook)<sup>6</sup>, rate-setting following a consolidation will not be addressed in a consolidation application unless the application possesses a rate proposal that is an integral aspect of the consolidation. Due to the unique circumstances of this Application, the Applicants have requested that approvals of MAADs and rates matters be considered and approved as part of this proceeding. Some overlap between MAADs and rates matters is unavoidable, although OEB staff has tried to minimize this to the extent possible.

## 1.2 Process to Date

The Applicants filed the Application on September 24, 2018 and requested a written hearing.

The OEB issued a Notice of Hearing on November 28, 2018. No parties filed for intervenor status.

In accordance with Procedural Order No. 1, OEB staff filed and served interrogatories on the Applicants, on January 15, 2019. The Applicants' responses to interrogatories were received by the OEB on January 28, 2019, and included one redacted response. A confidential, unredacted version of the response was provided to the OEB in accordance with the OEB's *Practice Direction on Confidential Filings*.

In accordance with the Decision on Confidentiality and Procedural Order No. 2, which was issued on February 6, 2019, the OEB will not require public disclosure of the redacted interrogatory response. The submission schedule was also established.

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<sup>4</sup> The APA has specifically excluded the Rue des Pins Substation, assets used or related to the lumber business of DLI, and any DLI customer-owned secondary assets. No employees, fleet, office facilities, or IT systems are included in the proposed transaction.

<sup>5</sup> Exhibit D/Tab 1/Schedule 1/p. 2

<sup>6</sup> [https://www.oeb.ca/oeb/Documents/Regulatory/OEB\\_Handbook\\_Consolidation.pdf](https://www.oeb.ca/oeb/Documents/Regulatory/OEB_Handbook_Consolidation.pdf)

### **1.3 Summary of OEB Staff's Position**

OEB staff submits that, for the elements in which the “no harm” test can be applied, API’s acquisition of the DLI distribution system meets the “no harm” test. OEB staff submits that the Applicants have demonstrated, where applicable given the unique context and considerations of the Application, that the proposed transaction will not adversely affect customers with respect to service quality and reliability. Further, OEB staff accepts the API’s assertion that the proposed transaction will not have a negative impact on API’s financial viability based on the price to be paid to acquire DLI’s distribution system. OEB staff accepts the business case set out by API that the transaction will be cost effective and efficient overall.

In light of API’s acknowledgement that the DLI distribution system is not currently in compliance with applicable regulatory requirements, OEB staff submits that including a specific time period for compliance with OEB Code provisions is a reasonable approach for the requested licence condition, but that any condition must be scoped to matters directly related to the management and operation of the existing DLI assets. OEB staff would expect API to proceed expeditiously with the work necessary to achieve compliance.

OEB staff supports the proposed approach to most rates issues; including classification of DLI’s customers within API’s existing rate structures, partial disposition on an interim basis of balances recorded in its OEB-approved Interim Distribution Licence Deferral Account, and establishment of a new deferral account to record transaction and integration costs incurred by API in lieu of a deferred rebasing period.

OEB staff is supportive of API’s proposed cost allocation approach at a high level and is supportive of the OEB including a limited endorsement in its decision. OEB staff does not find that a blanket endorsement of API’s proposed cost allocation methodology to be required or appropriate in light of the OEB’s expectations for API’s next cost of service application. The details of that methodology must be open to review at the next cost of service application.

**Part 1:**  
**OEB Staff Submissions Regarding MAADs-  
Related Elements**

## 2 RELEVANT REGULATORY PRINCIPLES

### 2.1 The “No Harm” Test

The OEB applies the “no harm” test when assessing applications for approval of utility consolidations. The “no harm” test was first established by the OEB in 2005 through its decision in an adjudicative proceeding (the Combined Proceeding),<sup>7</sup> and has been used to guide OEB decision making on MAADs applications since then.

The MAADs Handbook, issued by the OEB on January 19, 2016, confirmed that the OEB will continue its practice of applying the “no harm” test when adjudicating utility consolidation requests. The OEB considers whether the “no harm” test is satisfied based on an assessment of the cumulative effect of the transaction on the attainment of its statutory objectives. Those objectives include:<sup>8</sup>

#### **Board objectives, electricity**

1 (1) The Board, in carrying out its responsibilities under this or any other Act in relation to electricity, shall be guided by the following objectives:

1. To protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service.
  - 1.1 To promote the education of consumers.
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.
3. To promote electricity conservation and demand management in a manner consistent with the policies of the Government of Ontario, including having regard to the consumer’s economic circumstances.
4. To facilitate the implementation of a smart grid in Ontario.
5. To promote the use and generation of electricity from renewable energy sources in a manner consistent with the policies of the Government of Ontario, including the timely expansion or reinforcement of transmission systems and distribution systems to accommodate the connection of renewable energy generation

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<sup>7</sup> RP-2005-0018/EB-2005-0234/EB-2005-0254/EB-2005-0257

<sup>8</sup> *Ontario Energy Board Act, 1998*, Section 1

facilities. 2004, c. 23, Sched. B, s. 1; 2009, c. 12, Sched. D, s. 1; 2015, c. 29, s. 7.

If the proposed transaction has a positive or neutral effect on the attainment of these objectives, the OEB will approve the consolidation.<sup>9</sup>

## 2.2 OEB Policy on Rate-Making Associated with Consolidations

The OEB introduced policies that provide consolidating distributors with an opportunity to offset merger-related transaction costs with any achieved savings through deferral of the rebasing of the consolidated entity.

The OEB's policies on rate-making associated with consolidations are set out in the *Report of the Board – Rate-making Associated with Distributor Consolidation*<sup>10</sup>, issued July 23, 2007 (the 2007 Report) and a further report<sup>11</sup> issued under the same name on March 26, 2015 (the 2015 Report). The 2007 Report permitted a deferred rebasing period of five years. The 2015 Report extended the deferred rebasing period, permitting consolidating distributors to defer rebasing for up to ten years from the closing of the transaction.

Consolidating distributors are required to select a definitive timeframe for the deferred rebasing period. The OEB's expectation is that, when consolidating distributors select a deferred rebasing period, they have committed to a plan based on the circumstances of the consolidation and that, if an amendment to the selected deferred rebasing period is requested, the OEB will need to understand whether any change to the proposed rebasing timeframe is in the best interests of customers.

The OEB requires consolidating entities that propose to defer rebasing beyond five years to implement an earnings sharing mechanism (ESM) for the period beyond five years to protect customers and ensure that they share in any increased benefits from consolidation during the deferred rebasing period. In this case, API is proposing not to adopt a deferred rebasing period.<sup>12</sup> Instead, the Application notes that API is planning to apply to rebase its rates, through a cost of service application, for 2020, in accordance with the normal five-year schedule for the OEB's current Price Cap IR rate adjustment approach.<sup>13</sup> The new rates determined through the cost of service application would

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<sup>9</sup> MAADs Handbook, pp. 3-4

<sup>10</sup> [https://www.oeb.ca/documents/cases/EB-2007-0028/report\\_ratemaking\\_20070723.pdf](https://www.oeb.ca/documents/cases/EB-2007-0028/report_ratemaking_20070723.pdf)

<sup>11</sup> [https://www.oeb.ca/oeb/Documents/EB-2014-0138/Board\\_Report\\_MAADs\\_Ratemaking\\_20150326.pdf](https://www.oeb.ca/oeb/Documents/EB-2014-0138/Board_Report_MAADs_Ratemaking_20150326.pdf)

<sup>12</sup> Exhibit F/Tab 1/Schedule 1/pp. 1-3

<sup>13</sup> Exhibit E/Tab 2/Schedule 1/p. 4



apply to all API customers, including the former customers of DLI – pending approval of this Application and completion of the proposed transaction.

### **3 APPLICATION CONTEXT AND CONSIDERATIONS FOR MAADS MATTERS**

#### **3.1 API as DLI's Interim Distribution System Operator**

The Township was established in the early 1960s as a company town by Dubreuil Brothers Limited (DBL). In connection with its lumber operations, and to supply the Township with electricity, DBL developed, owned and operated the Township's electricity distribution system. The shares of DBL were amalgamated into Dubreuil Forest Products Limited (DFPL) in 1989.<sup>14</sup> However, in 2011, DFPL filed for bankruptcy, which resulted in the assets associated with the distribution system being transferred to DLI. On March 5, 2012, the OEB issued an Electricity Distribution Licence to DLI<sup>15</sup> for a term of one year. This licence, which was renewed annually until 2017, authorized DLI to own and operate the distribution system in the Township.

The OEB received letters from DLI on December 29, 2016 and February 17, 2017, advising that DLI would not be able to continue providing distribution service beyond April 27, 2017 due to financial and staffing issues. On April 4, 2017, the OEB appointed API as the interim operator for the DLI service area, and issued API an Interim Distribution Licence for this purpose.<sup>16</sup> Due to this, DLI was required to surrender possession and control of its distribution system. When issuing API an Interim Distribution Licence<sup>17</sup>, the OEB noted in its Order that for DLI to avoid falling into non-compliance with Section 57(a) of the Act, DLI shall renew its licence or dispose of its ownership interest in the DLI distribution system (whether through sale or transfer of its assets) to another licenced electricity distributor. Further, the OEB indicated that it was appointing an interim operator because DLI was likely to fail to meet its obligations related to the supply of electricity to its customers, and that it had selected API because API was DLI's host distributor and had experience working with DLI.

The OEB has since extended the term of the Interim Distribution Licence for additional six month periods, most recently<sup>18</sup> extending the term to April 2, 2019<sup>19</sup>.

As part of the April 4, 2017 Order<sup>20</sup>, API was required to provide the OEB with a Notice of Transition Report and a 60 Day Status Report. The purpose of these reports was to

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<sup>14</sup> Exhibit C/Tab 2/Schedule 1/p. 1

<sup>15</sup> ED-2012-0074

<sup>16</sup> EB-2017-0153

<sup>17</sup> EB-2017-0153

<sup>18</sup> EB-2018-0284

<sup>19</sup> The term of the Interim Distribution Licence was extended for a period of six months to April 2, 2019 or until the final determination of the Application, whichever is earlier.

<sup>20</sup> EB-2017-0153

provide the OEB with updates on the actions taken by API to assume operational control of the DLI distribution system. In addition, the reports highlighted concerns relating to metering and billing, health, safety and the environment, regulatory compliance, asset management, and reliability.<sup>21</sup> Since being appointed the interim operator, API has been addressing concerns outlined in the Notice of Transition Report and 60 Day Status Report in an effort to bring the DLI distribution system into regulatory compliance.

### **Submission**

In the Application, the Applicants “request that the OEB focus on different elements of its statutory objectives than it would in the circumstances of a more typical, efficiency-driven, consolidation transaction”.<sup>22</sup>

OEB staff agrees that this is not a typical MAADs application. API is the first holder of an Interim Distribution Licence under Section 59 of the Act to file an application for approval of the acquisition of the distribution system for which it has been appointed an interim operator. Further, during the time in which API has been appointed the interim operator, it has undertaken activities to remediate and bring the DLI distribution system into regulatory compliance.

The MAADs Handbook provides guidance to applicants and stakeholders on how the OEB reviews MAADs transactions proposed under Section 86 of the Act. As noted above in Section 2.1, the MAADs Handbook confirms that the OEB applies the “no harm” test in its assessment of MAADs applications. If the proposed transaction has a positive or neutral effect on the attainment of the OEB’s statutory objectives, the OEB will approve the application. While the OEB has broad statutory objectives, in applying the “no harm” test, the OEB has primarily focused its review on the impacts of the proposed transaction on price and quality of service to customers, and the cost effectiveness, economic efficiency and financial viability of the consolidating utilities.

As with any policy, the OEB can decide to not apply or to deviate from the policy if it determines that the circumstances warrant different treatment. OEB staff submits that the evidence filed highlights the unique circumstances of the proposed transaction and supports different treatment of the Application. For elements where the “no harm” test can be applied to the proposed transaction (i.e., service quality and reliability as well as financial viability), OEB staff submits that such tests still be applied to the proposed transaction. For non-standard elements of the Application (i.e., impact on price,

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<sup>21</sup> Exhibit B/Tab 1/Schedule 1/p. 6

<sup>22</sup> Exhibit B/Tab 1/Schedule 1/p. 5

economic efficiency and cost effectiveness), OEB staff submits that the OEB should adjudicate such elements exclusively for this Application.

OEB staff submits that the Applicants have demonstrated, where applicable given the unique context and considerations of the Application, that the proposed transaction will not adversely affect customers with respect to service quality and reliability. Further, OEB staff accepts the API's assertion that the proposed transaction will not have a negative impact on API's financial viability based on the price to be paid to acquire DLI's distribution system. OEB staff therefore submits, for elements in which the "no harm" test can be applied, that API's acquisition of the DLI distribution system meets the "no harm" test.

The basis for this conclusion is discussed in further detail below. OEB staff notes that matters related to price and cost-effectiveness are addressed in the following section and in the rates portion (Part 2) of this submission.

## **4 OEB STAFF SUBMISSIONS REGARDING “NO HARM” TEST**

In its review of the Application, OEB staff has considered the requirements described in the MAADs Handbook and other applicable OEB policy as described herein.

### **4.1 Impact on Price, Economic Efficiency and Cost Effectiveness**

The MAADs Handbook allows an acquiring or merging utility to elect, as part of the consolidation application, to defer rebasing for up to a maximum of ten years.<sup>23</sup> This deferral period is to allow the acquiring or merging utility an opportunity to recover transaction costs, which are not normally allowed to be recovered directly from customers, through operational and capital efficiencies resulting from the transaction over a reasonable period of time.

API proposes to not adopt a deferred rebasing period in the Application. Instead, it was noted in the Application that API plans to apply to rebase its rates, through a cost of service application for 2020, through the normal five-year schedule for the OEB’s current Price Cap IR rate adjustment approach. This approach of not adopting a deferred rebasing period has implications for price and economic efficiency; these elements, as well as OEB staff’s submissions on them, are discussed in Part 2 of this submission, at Section 7.3.

In the Application, API submitted that a focus on price, with regard to the “no harm” test, would be inappropriate given the OEB’s determination that DLI was likely to fail in meeting its obligation to supply electricity to customers in the Township. Due to the historical system condition and compliance issues, API has been, and will continue to be, required to make investments and improvements in the DLI distribution system.<sup>24</sup> Further, the Application stated that, historically, DLI did not file Reporting and Record Keeping Requirements (RRR) information with the OEB or segregate the financial records of its non-regulated business activities from those of its distribution business.<sup>25</sup> As a result, the Applicants noted that they are unable to provide a comparative analysis of the historical cost structures of both API and DLI.

Through the Application and its responses to interrogatories, API stated that it would be able to implement investments and improvements more efficiently and at a lower cost upon acquiring the DLI distribution system as compared to making such investments and improvements as the interim operator. Table 1, below, provides API’s estimates of

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<sup>23</sup> MAADs Handbook, p. 12

<sup>24</sup> Further discussion of this is contained in Section 7

<sup>25</sup> Exhibit E/Tab 2/Schedule 1/p. 1

the incremental costs associated with inefficiencies in the event that the proposed transaction does not proceed.<sup>26</sup>

**Table 1: Estimates of Incremental Costs Associated with Inefficiencies in the Event the Proposed Transaction Does Not Proceed**

Activity	Incremental One-Time Cost	Incremental Annual Cost
Changes to Enterprise Resource Planning system to establish and maintain DLI as a stand-alone entity	\$20,000	\$52,000
Regulatory: Stand-alone cost of service application, RRR filings, scorecards, IRM, etc.	Amortized over IRM rate-setting periods	\$57,000
Finance Department: Retain auditors and support annual audit, ongoing regulatory accounting, compile data for RRR reporting, rate applications, additional budgeting effort, support administration of service agreement, etc.		\$33,000
Establish and administer service agreement	\$2,000	Administration of inter-company billing captured under finance activities above
Engineering: GIS/OMS, Asset Management and System Planning, O. Reg. 22/04 processes and audits	\$1,000	\$50,000
<b>Total Estimated Incremental Costs</b>	<b>\$23,000</b>	<b>\$192,000</b>

***Submission***

OEB staff notes that its submissions on matters related to price are addressed in Part 2, at Section 7.3, in the rates portion of this submission. OEB staff anticipates that, in its first cost of service application following the sale of the DLI distribution system, API will demonstrate, where possible, any savings and efficiencies that have resulted from the acquisition. Savings and efficiencies in the proposed capital and operating costs may apply to API’s service area and customers, but API should try to identify any that are material and specifically due to the acquisition of DLI. Further, OEB staff accepts the business case set out by API that the transaction will be cost effective and efficient overall.

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<sup>26</sup> Response to Interrogatory OEB Staff-11

## 4.2 Impact on Service Quality and Reliability

The MAADs Handbook requires consolidating utilities to indicate the impact that the proposed transaction will have on consumers with respect to reliability and quality of electricity service. The MAADs Handbook also provides that in considering the impact of a proposed transaction on the quality and reliability of electricity service, and whether the “no harm” test has been met, the OEB will be informed by the metrics provided by the distributor in its annual reporting to the OEB and published in its annual scorecard.<sup>27</sup>

As noted in Section 3.1, the OEB appointed API as the interim operator to ensure service quality and reliability for customers in the Township.

OEB staff reviewed API’s 2017 Electricity Utility Scorecard and identified that the current and historical reliability metrics of API are fairly consistent based on the recent historical trend of API’s performance. The reliability metrics of API are shown in Table 2, below. As DLI did not historically file RRR information with the OEB, there are no System Average Interruption Frequency Index (SAIFI) and System Average Interruption Duration Index (SAIDI) statistics available for review for the DLI distribution system.

**Table 2: Historical SAIDI and SAIFI Performance for API**

Description	2013	2014	2015	2016	2017
SAIDI	7.00	7.96	8.80	5.46	7.68
SAIFI	2.94	3.24	3.68	2.57	3.95

API emphasized that significant improvements in service reliability and quality have been made to the DLI distribution system in the period since it became the interim operator in 2017. For example, the decommissioning of Rue des Pins Substation reduces the risk of extended outages to customers formerly served by this substation and addresses system loss and power quality issues related to operating the substation in an open-delta configuration.<sup>28</sup> In addition, API has been able to address unmetered and incorrectly metered loads which has reduced system losses. When questioned on approximately how much API has been able to reduce system losses in the DLI distribution system since becoming the interim operator, API noted that system losses have been reduced from 26% in 2017 to 15% in 2018.<sup>29</sup> Assuming the system loss factor had remained at 26% with 2018 delivery volumes, API estimates that approximately 750,000 kWh were saved in 2018.

<sup>27</sup> MAADs Handbook, p. 7

<sup>28</sup> Exhibit E/Tab 2/Schedule 1/p. 6

<sup>29</sup> Response to Interrogatory OEB Staff-14

In its interrogatories, OEB staff explored matters related to ensuring that the current reliability performance of the API and DLI distribution systems are not compromised by the proposed transaction. OEB staff sought clarity on how API will be able to ensure reliability for both existing API customers and former DLI customers given that API will be required to devote significant resources and efforts in the near term in order to bring the DLI distribution system into compliance. In response, API advised that in an effort to ensure that reliability for API's existing customers did not suffer as a result of devoting resources to these and other projects, API would use a mix of contracted services and temporary employees for future large-scale projects.<sup>30</sup> Further, API noted that it has already completed several projects required to bring the DLI distribution system into compliance and address high priority issues related to safety, environmental protection and reliability. Some of the examples highlighted included voltage conversion, installation of a bypass line and replacement of electromechanical meters with smart meters.<sup>31</sup>

### **Submission**

Based on the evidence provided, OEB staff submits that API can be expected to reasonably maintain and likely enhance the service quality and reliability of the DLI distribution system. As a result, OEB staff submits that the proposed transaction meets the "no harm" test with regards to service quality and reliability.

## **4.3 Impact on Financial Viability**

The MAADs Handbook provides that the impact of a proposed transaction on the acquiring utility's financial viability for an acquisition, or on the financial viability of the consolidated entity in the case of a merger, will be assessed. The OEB's primary considerations in this regard are:

- The effect of the purchase price, including any premium paid above the historic (book) value of the assets involved
- The financing of incremental costs (transaction and integration costs) to implement the consolidation transaction<sup>32</sup>

The proposed transaction involves API paying DLI a purchase price of \$45,000 and assuming DLI liabilities.

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<sup>30</sup> Response to Interrogatory OEB Staff-8

<sup>31</sup> *Ibid.*

<sup>32</sup> MAADs Handbook, p. 8



## **Submission**

OEB staff submits that the purchase price is a nominal amount (of which API is not seeking cost recovery) and therefore will not negatively impact the financial viability of API.

API has incurred, and will continue to incur, significant costs to remediate and operate DLI's distribution system. API has an established deferral account for tracking incremental one-time and ongoing costs while acting as interim operator<sup>33</sup>, and has proposed a new deferral account for tracking further costs until rebasing. Further discussion of the deferral accounts, the costs and the proposed disposition and recovery of these costs is provided in Part 2, Section 7.4, of this submission.

### **4.4 Limited Liability**

The Application requested that the OEB add a condition to provide API with limited relief from regulatory liability for circumstances arising from the acquisition of the DLI distribution system. In response to an interrogatory, it was clarified that API would consider the requested licence condition to be one element of a "Successful OEB Decision" for the purposes of the APA. It was further noted that if the condition was not included, API's Board of Directors may not proceed with the proposed transaction due to uncertainty with respect to regulatory compliance and the resulting risk of enforcement actions being contrary to the interest of API's customers and shareholders.<sup>34</sup>

Specifically, API has requested that the OEB refrain from the following:<sup>35</sup>

1. Issuing compliance orders under Section 112.3 of the Act.
2. Issuing orders suspending or revoking API's licence under Section 112.4 of the Act.
3. Issuing orders requiring payment of administrative penalties under Section 112.5 of the Act.
4. Alleging that API or any of its officers or directors have committed an offence under Part IX of the Act.

API stated, in response to an OEB staff interrogatory, that the requested condition for API's distribution licence would relate only to the DLI service area and only until all

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<sup>33</sup> Decision and Order, EB-2017-0135

<sup>34</sup> Response to Interrogatory OEB Staff-12(e)

<sup>35</sup> Response to Interrogatory OEB Staff-12(b)

deficiencies and potential compliance issues of the DLI distribution system are fully addressed.

When questioned by OEB staff on the timing of addressing all deficiencies, API's response noted that any specific circumstances or defects that API may be inheriting through the proposed transaction are not and cannot be fully known at this time. If the OEB were to allow a specified time period for compliance, API suggests that the OEB do so by including the requested licence condition, with a stipulation that the condition expires on a certain date, subject to the opportunity for API to apply to the OEB to extend the expiry date if needed.<sup>36</sup>

When asked to identify any precedent(s) that API is aware of for licences granted by the OEB which include a similar condition to provide a licensee with limited relief from regulatory liability, API cited its own Interim Electricity Distributor Licence<sup>37</sup>; and the Interim Electricity Distributor Licence<sup>38</sup> of Hydro One Networks Inc. (Hydro One) issued in respect of the system owned by Cat Lake Power Utility Inc.<sup>39</sup>

### **Submission**

In light of API's acknowledgment that the DLI distribution system is not currently in compliance with applicable regulatory requirements, and API's stated commitment to achieving compliance, OEB staff submits that allowing API a specified period in which to achieve compliance is reasonable. For the reasons discussed below, OEB staff suggest an alternative to the API request that the OEB refrain from enforcing certain provisions of the Act. OEB staff submit that this alternative is more consistent with the OEB's approach to compliance and enforcement. OEB staff is aware of the compliance issues and notes that API has demonstrated through its time as the interim operator that it has made efforts to identify and address deficiencies within the DLI distribution system on a timely basis.

OEB staff acknowledges that the API Interim Electricity Distributor Licence contains the following provision:

#### 9. Liability of the Licensee

The Licensee is not liable for anything that results from taking possession and control of the distribution assets owned by Dubreuil Lumber Inc. or otherwise exercising or performing the Licensee's powers and duties under the Act in

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<sup>36</sup> Response to Interrogatory OEB Staff-12(b)

<sup>37</sup> ED-2017-0153

<sup>38</sup> ED-2006-0181

<sup>39</sup> Response to Interrogatory OEB Staff-12(a)

relation to those businesses, this Licence or any order of the Board, unless liability arises from the Licensee's negligence or wilful misconduct.

OEB staff notes that that provision is derived from section 59(3.1) of the Act, which provides:

*Liability*

(3.1) A person who is required under clause (2)(a) to take possession and control of the business of a transmitter or distributor is not liable for anything that results from taking possession and control of the business or otherwise exercising or performing the person's powers and duties under this Act, the interim licence or any order of the Board, unless liability arises from the person's negligence or wilful misconduct.

This provision applies only to interim licensees. The Act does not explicitly provide for similar limitations of liability for holders of distribution licences other than those issued on an interim basis, although OEB staff acknowledges that Section 70 of the Act (dealing with licence conditions) provides that "A licence under this Part may prescribe the conditions under which a person may engage in an activity set out in section 57 and a licence may also contain such other conditions as are appropriate having regard to the objectives of the Board and the purposes of the *Electricity Act, 1998*; and that Section 70.1 of the Act (dealing with Codes that may be incorporated as licence conditions) contemplates the possibility of exemptions from OEB Codes. In the OEB's Order granting an interim licence<sup>40</sup> to API, DLI remained responsible for meeting all requirements under its current licence until the transfer is complete. Once the transfer of the DLI distribution system to API is complete, there is no other party other than API that would be liable for compliance with the OEB's Codes and licence conditions.

OEB staff submits that it would not be appropriate for the OEB to agree to "refrain" from carrying out its compliance and enforcement responsibilities under the Act with regard to the DLI system. Not even API is in a position to advise at this time as to the nature and scope of that system's non-compliance, although API has given some indications in its interrogatory responses.<sup>41</sup> Matters of compliance may arise in respect of the DLI system and its customers that are unrelated to the maintenance and operation of the DLI system assets, and the OEB should not be in a position in which it cannot investigate and require the resolution of those matters. However, OEB staff support the inclusion of a condition in the amended API Electricity Distributor Licence that would allow API time to bring the DLI system into compliance with OEB Code provisions in a

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<sup>40</sup> ED-2017-0153

<sup>41</sup> Response to Interrogatory OEB Staff-12(b)

manner more consistent with the OEB's compliance and enforcement role under the Act.

OEB staff understands that the requested condition would apply only to the DLI assets in service at the time of the completion of the transaction, and that it will not apply to other matters related to the administration of the utility, such as the implementation of the Ontario Electricity Support Program, the resolution of billing errors, or other statutory and/or OEB Code provisions that are not directly related to the management and operation of the existing DLI assets. OEB staff recommends the following text, which could be added as a new Schedule 4 to the amended API Distribution Licence:

The Licensee shall achieve compliance with those sections of the Codes set out in Section 5 of the Licence that pertain to the maintenance and operation of those assets in service in the former Dubreuil Lumber Inc. service area (as set out in former Electricity Distributor Licence ED-2012-0074 and Interim Electricity Distributor Licence ED-2017-0153) as of the date of the completion of the transfer of those assets from Dubreuil Lumber Inc. to the Licensee, by no later than December 31, 2024.

API has suggested that an appropriate expiry date would be December 31, 2024, a date coinciding with the end of API's next five-year planning cycle and rate-setting period. OEB staff agrees with the December 31, 2024 expiry date, and believes that the five-year time period would provide API with the opportunity to implement projects that are identified as priorities for the DLI distribution system, fully remediate and integrate the DLI distribution system into API's system, and enable flexibility for reprioritizing projects in the event that issues or circumstances arising from deficiencies need to be addressed. The requirement that API achieve compliance by that date is more consistent with the OEB's approach to compliance, in which it may issue compliance orders as contemplated by section 112.3 of the Act.

With respect to API's request that the OEB specifically recognize in the licence condition that API may apply for an extension of the compliance deadline, OEB staff submits that utilities generally have the ability to apply to the OEB for relief on various matters at any time. While it is conceivable that API may find that it needs additional time to achieve compliance, OEB staff submits that there is no need to explicitly allow API to apply for an extension. However, if the OEB were inclined to formally acknowledge API's ability to apply for an extension, then OEB staff recommends that this be added to the proposed licence condition set out above. This should not be construed as prejudging in any way the outcome of a request to extend the deadline. OEB staff would expect API to proceed expeditiously with the work necessary to achieve compliance.

**Part 2:**  
**OEB Staff Submissions Regarding Rates-Related  
Elements**

## 5 APPLICATION CONTEXT AND CONSIDERATIONS FOR RATES MATTERS

The rates for DLI have never been regulated by the OEB. DLI was a customer of API, and was charged API's rates as applicable to DLI (as a General Service > 50 kW customer). DLI in turn determined rates for customers in the Township such that it would recover the allocated portion of the bill charged to it by API, as well as DLI's own estimated system capital and operating costs, based on the metered consumption of each customer within the Township. Therefore, as API's rates, and also transmission and commodity costs, changed, DLI's rates also changed over time.

There are two other aspects of DLI's rate-setting which distinguish it from rate-regulated distributors in Ontario:

1. DLI did not unbundle its rates in the same way that rate-regulated Ontario electricity distributors did, whereby the distribution component of the bill was separated from transmission and commodity components. However, DLI did establish fixed and variable rates (to recover DLI distribution charges, as well as commodity and upstream transmission and distribution charges from API), and maintained slightly different rates for Residential and Commercial customers.
2. DLI was not subject to O. Reg. 424/06 and associated regulations (on the Smart Metering initiative in Ontario), and did not replace conventional meters with smart meters, as was required of all rate-regulated Ontario electricity distributors.

While DLI's rates were not regulated by the OEB, documentation provided by API illustrates that DLI's rate-setting approach tried to follow that used by the OEB in its Price Cap regulation of electricity distributors. In essence, DLI's distribution portion was subject to an annual inflation less productivity (I – X) approach based on the annually published parameters for the OEB. DLI also adjusted its rates monthly for the volumetric charge to reflect seasonal/monthly and price changes in transmission and commodity charges as passed on from API to DLI since DLI was a customer of API.<sup>42</sup> In its April 4, 2017 Order<sup>43</sup> appointing API as the interim operator, the OEB directed API to continue to charge rates in accordance with DLI's current structure. API confirmed this structure and its continued application, in response to an OEB staff interrogatory.<sup>44</sup>

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<sup>42</sup> Response to Interrogatory OEB Staff-3, Schedule 3(a) providing a summary of DLI's rates as calculated and updated monthly for 2017 and 2018 as charged by API to DLI customers.

<sup>43</sup> EB-2017-0153

<sup>44</sup> Response to Interrogatory OEB Staff-3

DLI was treated as a customer of API subject to Rural or Remote Electricity Rate Protection (RRRP),<sup>45</sup> similar to API's own Residential and General Service < 50 kW customers, in accordance with O. Reg. 442/01. DLI's approach to allocating those charges and passing them on to other Residential and Commercial customers in the Township meant that all customers were implicitly afforded RRRP treatment.

As API noted, DLI's rates are not compensatory for API's costs for investment in and operation of DLI's system at applicable standards, should the acquisition be approved and completed. API, along with third-party engineers and other agencies (e.g., the Electrical Safety Authority), have inspected the DLI distribution system and identified deficiencies. Since being appointed the interim operator, API has been taking steps to remediate the DLI distribution system to ensure that it complies with all applicable codes. API has documented these findings and efforts in reports<sup>46</sup> filed with the OEB, as required, during the time it has been interim operator of the DLI distribution system.<sup>47</sup>

API is tracking capital and operating costs associated with the transaction and integration, and is seeking partial recovery now from all DLI customers, and the remainder later as part of an expected cost of service application by API to rebase its distribution rates.

If the proposed transaction is approved, and API fully integrates DLI's rehabilitated distribution system into its own operations, the costs for serving DLI's customers will be similar to, and indistinguishable from, those of other API customers. However, API's costs will be greater to invest and operate DLI's distribution system to ensure it meets applicable standards for safety, reliability, etc. For instance, the installation of smart meters in the DLI distribution system, together with the installation and operation of the associated communications systems for those smart meters,<sup>48</sup> will increase the capital costs of the network in the Township. The capital costs are greater, and the expected useful life is shorter, than for conventional meters, meaning that the revenue requirement related to the Township area will be higher on an annual (or monthly) basis. However, DLI customers will benefit from the infrastructure and operational improvements made by API.

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<sup>45</sup> Per O. Reg. 445/07. See Exhibit C/Tab 1/Schedule 1/p. 5

<sup>46</sup> Notice of Transition, provided in Exhibit C/Tab 2/Schedule 1/Appendix B and 60-day Status Report, provided in Exhibit C/Tab 2/Schedule 1/Appendix C

<sup>47</sup> See Exhibit E/Tab 1/Schedule 1 and Exhibit E/Tab 1/Schedule 2, wherein API describes its efforts to date and going forward to address DLI distribution system issues regarding safety, reliability, operations and customer service.

<sup>48</sup> Advanced Metering Infrastructure or AMI.

## **Submission**

The OEB's policy with respect to consolidations is that rates considerations are not dealt with or approved as part of a consolidation application, except in circumstances where the rates matter is an integral factor in the proposed acquisition or merger.<sup>49</sup> Reconfirmed in recent consolidation policy documents,<sup>50</sup> this approach dates back to the initial consolidation policy<sup>51</sup> established following restructuring under Bill 35.

API has requested changes to rates applicable to DLI customers along with approval of the acquisition of DLI's distribution system. In the Application, API has provided reasons for this proposed approach. As with any policy, the OEB can decide to not apply, or to deviate from, the policy if it decides that the circumstances warrant different treatment.

OEB staff notes that while there may be other examples<sup>52</sup> of cases that are instructive in regard to the OEB considering rates and MAADs applications together, there is one case specifically that is the most relevant:

- Enbridge Gas Distribution Inc.'s (Enbridge) acquisition of Wellandport Gas Company Limited (Wellandport)<sup>53</sup>

In Enbridge's acquisition of Wellandport, Enbridge noted that it would incur additional costs to remediate Wellandport's system up to code and integrate it and Wellandport's customers into its system. Enbridge did not seek direct recovery of the costs, but requested approval to recover the purchase price premium in addition to the net book value of the acquired assets. That request was approved by the OEB. OEB staff considers the Wellandport case to be similar to the current Application, in that in this case, the acquiring utility, API, will incur what are anticipated to be significant costs in order to remediate the acquired DLI distribution assets.

OEB staff submits that the request to consider both API's acquisition of DLI's distribution system and API's rate request is reasonable in light of the circumstances and when considered in light of the earlier noted case. OEB staff also notes that the

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<sup>49</sup> MAADs Handbook, pp. 6-7

<sup>50</sup> Consolidation Handbook and MAADs Handbook, *op. cit.*

<sup>51</sup> RP-1999-0036, *Preliminary Filing Requirements for Mergers, Acquisitions, Amalgamations, and Divestitures in the Ontario Electricity Transmission and Distribution Sector*, and *A Guide to the Preliminary Filing Requirements for Mergers, Acquisitions, Amalgamations, and Divestitures in the Ontario Electricity Transmission and Distribution Sector*, both issued February 9, 2000. Subsequent to this, Decision RP-2005-0018/EB-2005-0234/EB-2005-0254/EB-2005-0257 and the *Report of the Board on Rate-making Associated with Distributor Consolidation*, July 23, 2007 also reconfirmed that, while future intentions on rate-making should be provided in MAADs applications, decisions on rates should be limited as parts of MAADs applications.

<sup>52</sup> Hydro One Networks Inc.'s acquisition of Terrace Bay Superior Wires Inc., EB-2007-0666/EB-2007-0688/EB-2007-0726/EB-2007-0727

<sup>53</sup> RP-2002-0106



OEB's Notice of Application documented both the proposed MAADs and rates approvals being sought in the Application, which API has stated is a requirement in order to conclude the transaction including the proposed rate treatment and recovery of some of the costs API has incurred as the interim operator of DLI's distribution system.

## 6 RELEVANT REGULATORY PRINCIPLES

### 6.1 Tests for Rates-Related Matters

The OEB's authority related to rate-setting in the Ontario electricity sector is provided under Section 78 of the Act. In carrying out its responsibilities under Section 78 of the Act and other applicable legislation and regulations, the OEB must consider its objectives as set out in the Act. These objectives are provided earlier in this submission.<sup>54</sup> While the OEB must consider all of the objectives, objectives one and two are the most relevant in the context of the rates-related aspects of this Application.

#### ***Submission***

OEB staff notes that the Applicants, specifically API, have not requested changes in rate-setting methodology or changes to API's current OEB-approved rates. Instead, API has requested application of API's rates to DLI customers upon closing of the proposed transaction, and treatment in this Application and at the time of API's next rate rebasing application, for legitimate and reasonable costs associated with API's remediation and operation of DLI's distribution system and integration into API's network and operations, as discussed in Section 7.4.

OEB staff submissions on rates-related matters are made with these considerations in mind. OEB staff submits that it is largely objectives one and two, referenced above, that OEB staff considered in making the following submissions on rates-related matters of the Application.

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<sup>54</sup> See Section 2.1

## 7 OEB STAFF SUBMISSIONS REGARDING RATES

In its review of the Application, OEB staff has considered the requirements described in the MAADs and Rate Handbooks and other applicable OEB policy as described herein.

### 7.1 Rural or Remote Electricity Rate Protection

As noted above, DLI's customers implicitly are afforded RRRP treatment as contemplated in O. Reg. 442/01. API proposes that, after the acquisition, if approved, DLI customers will be afforded RRRP protection as Residential and General Service < 50 kW customers under API's approved Tariff of Rates and Charges.<sup>55</sup> As a result, there will be no material change in the RRRP-treatment for most of DLI's customers. API has noted that street lights and possibly some other unmetered loads will have to be addressed by the time of API's cost of service rebasing application, as these unmetered customers were also unbilled by DLI.<sup>56</sup> Further, API documents that all Commercial customers in the Township are being classified as General Service < 50 kW. Poor meter data prevents identification of any Commercial customers who may qualify for the General Service > 50 kW class, at which point they would not qualify for RRRP treatment. This may have larger bill impacts for any such customers, but cannot be identified at this time. API advises that information may be available by the time of API's expected 2020 rebasing application due to improved meter data.

API advised that the addition of DLI's customers – approximately 353 customers (representing an addition of about 3% to API's existing customer base) – will not materially impact the eligibility of API's Residential and General Service < 50 kW customers in the R1 and R2 rate classes. This is because API's customer density per square kilometer, following the acquisition of the DLI distribution system, would remain below the threshold of seven customers per kilometre of distribution line as specified in O. Reg. 442/01, meaning that API's Residential and Small Commercial customers would remain eligible for RRRP.<sup>57</sup> Consequently, the proposed transaction resulting in API acquiring DLI customers would not impact other API customers directly.

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<sup>55</sup> Residential customers are classified as R1, and Small Commercial (General Service < 50 kW) customers are classified as R2, under API's approved Tariff of Rates and Charges.

<sup>56</sup> DLI charged rates to only its Residential and Small Commercial classes. There were no discrete rates for unmetered loads as DLI absorbed these costs as part of its power consumption for its own operations (which dated back to when the Township was a company town of the lumber mill). See Exhibit E/Tab 2/Schedule 1/pp. 5-6 and footnote 3 on page 6 that streetlights currently in the Township are "unmetered and unbilled".

<sup>57</sup> Exhibit C/Tab 1/Schedule 1/p. 5/Footnote 4

**Submission**

With the exception of the requested endorsement of API’s cost allocation methodology for the next cost of service rebasing application as discussed in Section 7.5, OEB staff takes no issue with the assignment of DLI’s Residential and all Commercial customers to API’s R1 and R2 classes, and eligibility under RRRP.

**7.2 Bill Impacts from Moving DLI Customers to API’s Approved Tariff of Rates and Charges**

API provided estimated bill impacts showing the effect of moving DLI customers to API’s rates versus API continuing operations as an interim operator of DLI’s distribution system, including incremental costs recorded in the current deferral account that API proposes for partial disposition in this Application.<sup>58</sup> In addition to the original bill impacts shown in the Application,<sup>59</sup> API provided updated bill impacts against API’s recently approved 2019 rates in response to an OEB staff interrogatory.<sup>60</sup>

The following table summarizes the estimated bill impacts based on API’s approved 2019 Tariff of Rates and Charges:<sup>61</sup>

**Table 3: Detailed Bill Impact Calculations for DLI Customers Upon Transitioning to API’s 2019 Rates**

<b>Rate Class</b>	<b>Monthly Consumption (kWh)</b>	<b>Total Bill – API Interim Operation</b>	<b>Total Bill – Proposed Transaction</b>	<b>\$ Change</b>	<b>% Change</b>
Residential <sup>4</sup>	393	\$ 103.22	\$ 92.16	-\$11.06	-10.7%
Residential <sup>4</sup>	750	\$ 147.65	\$ 129.30	-\$18.35	-12.4%
Commercial	2000	\$ 320.40	\$ 340.56	\$ 20.16	6.3%

<sup>58</sup> See Section 7.4

<sup>59</sup> Exhibit F/Tab 2/Schedule 1/Appendix B

<sup>60</sup> Response to Interrogatory OEB Staff-7 and Schedule 7(b)

<sup>61</sup> *Ibid.* Footnote 4: The residential cases remain unchanged from the [A]pplication, despite a reduction of \$0.11 in API’s approved 2019 monthly service charge as compared to the [A]pplication. This is because in both cases, the total distribution charges exceed the cap of \$36.86 under the Distribution Rate Protection (DRP) program. While the total bill impact remains unchanged, the \$0.11 difference can be seen in comparing the “Effect of DRP” line of the detailed bill impact calculations in Schedule 7b to those provide in Exh. F-2-1, Appendix B of the [A]pplication.

In the Application, API explained that acquired Residential customers, regardless of consumption levels, would see a reduction of their total electricity bill as a result of the proposed transaction, mainly driven by the effect of the Distribution Rate Protection (DRP) cap on distribution rates.<sup>62</sup> Conversely, Commercial customers would see an increase in their total electricity bill as they would be ineligible for DRP. However, the resulting bill impact for Commercial customers is below the threshold that would normally require mitigation.

### **Submission**

While the evidence that API has provided is not exactly a comparison against DLI's existing rates, OEB staff agrees with the Applicants that the comparison of the bill impacts of DLI's rates to the bill impacts of API rates would be misleading as DLI's rates would not be compensatory to API. Further, OEB staff submits that DLI customers are receiving service improvements through API's investments and operations; and, as such, it would not make sense to continue with DLI's existing rates.

OEB staff submits that API's proposal that DLI customers be migrated to API's R1 and R2 classes, as applicable, upon completion of the proposed transaction is reasonable. With the improvements in the infrastructure and operations, DLI customers are receiving, and will continue to receive, improved service in line with that experienced by API's existing customers. This request to change rates at the time of the acquisition is not standard, but OEB staff agrees with API that the unique circumstances of the proposed transaction warrant unique consideration.

Having to maintain separate rates, even if the proposed acquisition is approved, would result in additional costs and complexity for API, costs which would ultimately have to be borne by ratepayers. At this point, the differences between DLI's rates and those of API in recovering the costs of serving their respective customers are related more to the age and the condition of DLI's distribution system (which API is remediating) and poor record-keeping.

OEB staff supports API's proposal that DLI customers be charged API's current approved rates upon completion of the proposed acquisition.

## **7.3 No Deferred Rebasing Period**

The MAADs Handbook allows an acquiring or merging utility to elect, as part of the consolidation application, to defer rebasing for up to a maximum of ten years.<sup>63</sup> This

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<sup>62</sup> Exhibit F/Tab 2/Schedule 1/p. 4

<sup>63</sup> MAADs Handbook, p. 12

deferral period is to allow the acquiring or merging utility an opportunity to recover transaction costs, which are not normally allowed to be recovered directly from customers, through operational and capital efficiencies resulting from the transaction over a reasonable period of time.<sup>64</sup>

In this Application, API is proposing to not adopt a deferred rebasing period. Instead, API is planning to apply to rebase its rates, through a cost of service application, for 2020, in accordance with the normal five-year schedule for the OEB's current Price Cap IR rate adjustment approach. This will enable API to reset its rates for all API customers based on updated load forecasts (which would include the addition of DLI customers), associated demand, capital and operating costs, an updated Distribution System Plan, and updated cost allocation and rate design data and proposals.

API notes in the Application that it will seek additional approval in its 2020 rate application for recovery of remaining incremental costs incurred as interim operator to operate and remediate DLI's distribution system, and similar incremental costs incurred after the completion of the transaction to complete the refurbishment of the DLI distribution system.

API also highlights that the synergies normally expected to result from a consolidation – a key reason why most consolidation applicants have negotiated such a transaction and seek the necessary regulatory approval(s) – are not present in the proposed transaction and API is therefore not seeking a deferral of rebasing.<sup>65</sup> API was appointed as the interim operator when DLI informed the OEB that it would not be able to continue to effectively operate its distribution system as its revenues were no longer sufficient to cover costs and that significant investment is needed.

### **Submission**

OEB staff acknowledges that synergies are not a key driver of the proposed transaction. However, as API has documented, integration of DLI's distribution system into API's system should result in some synergies, as noted in Section 4.1. Back office systems (e.g., billing and collections; meter reading, once smart meters and AMI communications are deployed and in-service; etc.) should not require any material expansion to accommodate the 3% increase in customers, and API's corporate office

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<sup>64</sup> Not allowing transaction costs, or a revaluation of assets, due to a merger or acquisition, is the normal policy for the OEB and, to the best of OEB staff's knowledge, for most other regulators, especially in North America. However, exceptions can be allowed. Enbridge's acquisition of Wellandport (discussed earlier) is one such case, where the OEB allowed the purchase price premium paid by Enbridge to be recouped in light of the investments committed to by Enbridge to refurbish the small and older Wellandport gas infrastructure up to code and integrate it into Enbridge's system, thereby improving the service provided to Wellandport customers, particularly with respect to reliability and safety.

<sup>65</sup> Exhibit F/Tab 1/Schedule 1/p. 2

functions will be recoverable over a slightly larger customer base. With adoption of common plant (poles, transformers, conductor, meters), design, operations and inspection, and procurement, API should see some efficiencies relative to the increase in customers. Better use may be made of API's operations centre in Wawa in serving a slightly larger network and number of customers in the northern part of API's service territory as well. However, OEB staff submits that any synergies may be relatively small, corresponding to the small increase in customers and assets for API as a result of acquiring DLI's distribution system.

API proposed a new deferral account to record further incremental costs for remediation of the DLI distribution system post-closing of the transaction. This matter is discussed in Section 7.4. API will apply to rebase its rates for all of API's customers for 2020. No approval is required for the selection of a deferral period (even if that selection is to not defer at all), OEB staff notes that rebasing for 2020 rates will give API more certainty of cost recovery. It will allow the OEB panel adjudicating that application to have the necessary information and allow it to be assessed on a timely basis.

## **7.4 Deferral Account**

In the Order<sup>66</sup> appointing API as the interim operator of the DLI distribution system, the OEB established a deferral account for two purposes:

1. To track the incremental capital and operating costs that API incurred as part of its operation of the DLI system under the Interim Distribution Licence.
2. To track the revenues that API recovered from the Township customers being billed according to DLI's existing rates.

The account is the Interim Distribution Licence Deferral Account. API has provided further description of this account in its Application<sup>67</sup> and provides the following table of historical actuals and forecasted costs:

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<sup>66</sup> EB-2017-0153

<sup>67</sup> Exhibit F/Tab 3/Schedule 1/Section A

**Table 4: Historical Actuals and Forecasted**

Nature of Costs	Description	2017 Actual	2018 YTD (Jan-Jun)	2018 Forecast (Jul-Dec)	2018 Forecast	2019 Forecast
OM&A, Cost of Power, Billed Revenue	Outage and Emergency Response (Includes Locates)	51,999	40,214	40,214	80,428	80,428
	Meter Reading	54,552	18,351	18,351	36,702	36,702
	Customer Service and Community Relations	16,498	529	5,000	5,529	5,000
	Billing & Collections	22,770	4,367	4,367	8,734	8,734
	Supervisory and Administrative Support	7,014	2,126	2,126	4,252	4,252
	Cyclical Maintenance	-	-	6,500	6,500	10,000
	Cost of Power and Billed Revenue Tracking	8,062	28,435	28,435	56,870	126,823
	<b>Sub-Total OM&amp;A, Cost of Power, Billed Revenue</b>	<b>160,895</b>	<b>37,151</b>	<b>48,123</b>	<b>85,274</b>	<b>18,292</b>
Capital	Distribution Line Capital (Including Bypass Project)	149,108	14,138	110,000	124,138	252,000
	Metering Replacements	-	-	118,140	118,140	-
	Substation and Underground Capital	-	-	33,859	33,859	250,000
	<b>Sub-Total Capital</b>	<b>149,108</b>	<b>14,138</b>	<b>261,999</b>	<b>276,137</b>	<b>502,000</b>
One-Time	Transfer of Control and Process Development	51,086	3,664	5,000	8,664	-
	Condition Assessments, Audits, and Reporting	63,065	53,196	10,000	63,196	-
	Safety, Environmental and Regulatory Compliance	19,466	14,447	-	14,447	-
	Substation #1 Decommissioning	-	-	67,453	67,453	-
	Substation #2 Transformer Contingency	-	-	15,000	15,000	-
	Oil Sampling for PCB Testing	-	-	-	-	80,000
	<b>Sub-Total One-Time Costs</b>	<b>133,617</b>	<b>71,307</b>	<b>97,453</b>	<b>168,761</b>	<b>80,000</b>
<b>Total</b>	<b>443,619</b>	<b>122,596</b>	<b>407,576</b>	<b>530,172</b>	<b>600,292</b>	

API is requesting disposition of this deferral account, on an interim basis. In the Application, “API proposes to recover the following costs through a monthly fixed rate rider that would apply to all [a]cquired [c]ustomers:

- 50% of the 2017 total [net amount] of OM&A, Cost of Power and Billed Revenue
- 100% of the 2018-2019 total [net amount] of OM&A, Cost of Power and Billed Revenue
- Amortization expense and return on capital for the 2017-2019 period
- Tax impacts associated with the above costs
- The net impact of the simple interest calculated on cumulative OM&A and amortization expense offset by the simple interest calculated on revenues from the resulting rate rider.”<sup>68</sup>

API has proposed that the rate rider that it is seeking approval for in this Application be based on the approach similar to that which the OEB established for recovery of smart meter costs.<sup>69</sup> API consulted with OEB staff and has used a modification of the OEB-issued Smart Meter Model to determine the amount requested for disposition and the rate riders to recover it; API refers to this as the “API-DLI Rate Model”.<sup>70</sup> API filed a

<sup>68</sup> Exhibit F/Tab 3/Schedule 1/Section B/p. 2

<sup>69</sup> Specifically, this refers to the approach to record reasonable incremental capital and operating costs over a multi-year period, for subsequent recovery after review through rate riders to recover the deferred incremental revenue requirement from customers. This was adopted by the OEB in Decision with Reasons EB-2007-0063 (August 8, 2007), and then expanded on in *Guideline G-2008-0002: Smart Meter Funding and Cost Recovery* (October 22, 2008) and then *Guideline G-2011-0001: Smart Meter Funding and Cost Recovery – Final Disposition* (December 15, 2011) and the associated OEB-issued Smart Meter Model.

<sup>70</sup> Exhibit F/Tab 3/Schedule 1/pp. 3-4



copy of the model in working Microsoft Excel format. API has reflected the proposed rate riders in the estimated bill impacts on DLI customers.

One-time costs, and 50% of the 2017 OM&A expenses would be transferred to the proposed new deferral account, the Transaction and Integration Costs Deferral Account, for review and disposition as part of the next cost of service application. API has proposed an effective date of April 4, 2017 for the new deferral account (the date API assumed interim operation of DLI's distribution system).<sup>71</sup> In addition to recording amounts transferred from the Interim Distribution Licence Deferral Account, API would use this account to record one-time costs incurred post-closing until the balances are reviewed and disposed of at the next cost of service rebasing application. API has provided a table detailing the costs proposed in this new deferral account in its Application:<sup>72</sup>

**Table 5: Transaction Costs**

Description	2017 Actual	2018 Forecast	2019 Forecast	Total
Transaction Costs	-	83,674	85,000	168,674
Transfer of One-Time Costs from Deferral Account	133,617	71,307	97,453	302,377
Transfer of 50% of 2017 OM&A from Deferral Account	80,447			80,447
<b>Total Transaction and Integration Costs</b>	<b>214,064</b>	<b>154,981</b>	<b>182,453</b>	<b>551,499</b>

A draft Accounting Order is included in the Application.<sup>73</sup>

**Submission**

OEB staff submits that API's proposals for the existing and new deferral accounts, and the treatment of amounts recorded and to be recorded in these accounts, are reasonable and consistent with OEB policies and with the April 4, 2017 Order.<sup>74</sup> OEB staff also submits that API's proposals for partial interim disposition and recovery of 2017 costs, and the rate riders to recover these amounts, are reasonable.

Partial disposition at this point, on an interim basis, may also serve to mitigate bill impacts faced by DLI customers now and at the time of API's next application to rebase rates. At the time of that application, the OEB will have an opportunity for a comprehensive review of documented costs in the new deferral account prior to determining amounts eligible for final disposition. Based on the evidence in the

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<sup>71</sup> Per Order EB-2017-0153  
<sup>72</sup> Exhibit F/Tab 3/Schedule 2/p. 6  
<sup>73</sup> Exhibit F/Tab 3/Schedule 2/p. 4/Appendix A  
<sup>74</sup> Order EB-2017-0153, *op. cit.*

Application, OEB staff submits that the partial disposition requested by API on an interim basis is reasonable. OEB staff also submits that this proposed partial disposition is similar to the treatment afforded to smart meter costs in applications seeking partial cost recovery in accordance with OEB-issued guidelines.<sup>75</sup>

## 7.5 Endorsement of API's Proposed Cost Allocation Methodology

As noted earlier, in its Application, API requests “that the OEB endorse its proposed approach of allocating costs attributable to the DLI service area, at the time of API's next rebasing, primarily to API's R1 and R2 rate classes, which are eligible for Rural or Remote Electricity Rate Protection”.<sup>76</sup> This is not a typical request in a MAADs (or Rates) application. OEB staff sought additional explanation of this request, regarding its nature, if it is integral to the proposed MAADs transaction (i.e., to any clause in the APA),<sup>77</sup> and on precedents for this request through an interrogatory.<sup>78</sup>

In its response, API provided further explanation. It pointed to Section 3.5(c) of the APA:

If the OEB determines that API's request – for the Board to endorse its plans to allocate costs related to the DLI service area in a manner that mitigates bill impacts to API's existing customers – is not appropriate, then API would not have a reasonable expectation of being able to recover its costs in a manner that results in no harm to its existing customers. As such, API's Board of Directors may consider that proceeding with the Proposed Transaction is contrary to the interests of its existing customers, and could therefore decide not to proceed with the Proposed Transaction in accordance with s. 3.5(c) of the APA and the definition of “Successful OEB Decision” thereunder. See also response to Board Staff IR 13.<sup>79</sup>

API's arguments are focused on the fact that Street Lighting and Seasonal customers are not subject to RRRP, and that the addition of allocated costs for such customers in the Township could result in upward pressure on the rates for API's existing customers in those classes.<sup>80</sup>

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<sup>75</sup> See Footnote 64

<sup>76</sup> Exhibit B/Tab 1/Schedule 1/p. 4. Further discussion was also provided in Exhibit E/Tab 2/Schedule 1/pp. 5-6.

<sup>77</sup> Exhibit D/Tab 1/Schedule 1/Appendix A

<sup>78</sup> Interrogatory OEB Staff-1

<sup>79</sup> *Ibid.*, Response (b)(i)

<sup>80</sup> Exhibit E/Tab 2/Schedule 1/pp. 5-6 and Response to Interrogatory OEB Staff-1.

API refers to the OEB's Decision and Order in Hydro One's application to acquire the shares of Orillia Power Distribution Corporation (Orillia Power)<sup>81</sup> regarding recent interest in the matter of future rates, including cost allocation, for the OEB panel's consideration in this MAADs application.<sup>82</sup> API also acknowledged that a finding of one panel cannot bind another panel in a future case.

### **Submission**

OEB staff considers API's request to be a request for a blanket endorsement of API's approach to its next cost allocation study. While there is a question as to what any such endorsement means for API's next cost of service application, in OEB staff's view, API should in fact be proposing an approach that considers all of its existing customers (especially low volume customers), in addition to its acquired customers, when allocating costs attributable to the DLI service area at the time of API's next rebasing. OEB staff further submits that API should consider the current deferral account, the time that is required to bring the DLI distribution system up to acceptable standards on a permanent basis, and any efficiencies that will benefit the entire utility (among other factors) when considering its allocation of costs. However, for the reasons set out below, the specific details of API's cost allocation must be reviewed in the next cost of service application.

The Applicants have quoted from the decision in the Hydro One-Orillia Power MAADs proceeding as a recent precedent of the OEB's interest in rates matters in a MAADs application as support for its requested blanket endorsement. OEB staff notes that API's own experience in its most recent rebasing application is likely more relevant than what the OEB may have stated in other, unrelated cases, as discussed further below. API indicates that it is currently not aware of Seasonal customers in the Township.<sup>83</sup> OEB staff submits that API's concerns with respect to the Seasonal customer class are therefore hypothetical at this point as there are no Seasonal customers in the DLI service area. Therefore, there are no costs of serving the Seasonal customers in the DLI service area that would be allocated to API's existing customers in this class.

API documents that there are approximately 50 street lights in the Township.<sup>84</sup> Many, if not all, of these may have benefited as unmetered services for which the costs of serving were (largely) borne by DLI based on the Township's history as a company town of the forestry business. OEB staff acknowledges that there may be an issue with

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<sup>81</sup> EB-2016-0276

<sup>82</sup> Response to Interrogatory OEB Staff-1(a)

<sup>83</sup> Response to Interrogatory OEB Staff-1(b)(ii)

<sup>84</sup> *Ibid.*

incremental costs being allocated to existing API street lights but, as discussed below, there are questions as to whether this is material.<sup>85</sup>

Additionally, while API appears to be seeking a blanket endorsement as a means of reducing risk, OEB staff notes the OEB has already directed that an updated cost allocation study be filed in the next API cost of service application and the matter of how Street Lighting and Seasonal customers will be treated in that study will be a matter for that proceeding. Following from the Decision and Order<sup>86</sup> on API's last cost of service rebasing application, the OEB stated the following regarding revenue-to-cost ratios for Seasonal and Street Lighting rate classes:

The issue of revenue-to-cost ratios for Algoma Power differs in scope from those of other distributors as a consequence of its eligibility for the RRRP. Unlike other distributors, any distribution rate increase for Algoma Power's R1 and R2 classes is capped by regulation at the provincial average rate increase (the RRRP Adjustment Factor). Any remaining cost from Algoma Power's R1 and R2 classes is collected through the RRRP. ***In addition, if the Seasonal and Street Lighting rate classes have ratios lower than 100%, the difference is also collected from all Ontario electricity customers who fund RRRP. [Emphasis added.]***<sup>87</sup>

In its findings, the OEB stated:

The Board finds it appropriate to maintain the current fixed-variable rate splits in 2015 for the Seasonal and Street Lighting classes. The Board does not agree that test year rate design should be based on previous settlement considerations and negotiations, especially given a potential four year subsequent IRM period. In addition, the Board does not support maintaining fixed rates at current levels as a means to lower total bills for low-volume Seasonal and Street Lighting customers. The Board directs Algoma Power to maintain the current fixed-variable splits for the Seasonal and Street Lighting rate classes until a new cost allocation study is complete and rate designs are proposed.<sup>88</sup>

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<sup>85</sup> *Ibid.* API states that residential and commercial customers represent 99.8% of the accounts and "virtually 100% of the load" in the Township, which suggests that few costs would be apportioned to streetlights in the Township. With addition of DLI customers and assets representing only about a 3% addition to API's customers and rate base, it is unlikely, in OEB staff's view, that costs allocated to API's Street Lighting class would be affected in any material and adverse manner as a result of the transaction.

<sup>86</sup> EB-2014-0055

<sup>87</sup> Decision and Order EB-2014-0055, January 8, 2015, p. 8

<sup>88</sup> *Ibid.*, p. 12

With a complete record of cost allocation in accordance with the OEB's policies in that case, the OEB recognized issues on allocated costs on all classes, including Street Lighting, the remedies available through RRRP, and made its findings for that case that afforded some protection to the Street Lighting class, including establishing a requirement that API undertake an updated cost allocation study to be filed and considered in the next cost of service application. Thus, the extent to which the Street Lighting class for example, will continue to be protected through a cost allocation exercise is a matter that the OEB has already indicated will be addressed in the next cost of service application. It is possible that there may be upward pressure on API's Street Lighting customers to address adjustments in revenue-to-cost ratios and inflation (less productivity), together with the addition of DLI's costs. However, it is not clear from the record of this current proceeding that DLI-related impacts will be material, or that existing remedies<sup>89</sup> would not suffice to address any impacts.

In light of the foregoing, OEB staff submits that there does not appear to be a need for a blanket endorsement at this time. OEB staff agrees that API's proposed approach appears to be reasonable as a starting point. OEB staff does not have any concerns if the OEB was to state this position as way of providing a limited endorsement in an effort to provide API with some comfort that what it is proposing is directionally acceptable. However, this support would not bind a future panel reviewing the outcomes of the updated cost allocation study, nor would it bind OEB staff or prevent staff from taking a different position, as part of API's next cost service application.

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<sup>89</sup> e.g., the RRRP availability described on p. 8 of Decision and Order EB-2014-0055, or standard rate mitigation per OEB rate policies.

## 8 CONCLUSION

The Applicants have requested the OEB's approval for:

- DLI's proposed sale of its electricity distribution system, substantially in its entirety, to API
- Cancellation of DLI's Electricity Distribution Licence
- Cancellation of API's Interim Distribution Licence to operate DLI's distribution system
- Amendment of API's Electricity Distribution Licence by:
  - Adding the Township of Dubreuilville to the description of the service area in which API is authorized to distribute and sell electricity
  - Adding a condition to provide API with limited relief from regulatory liability for circumstances arising from its acquisition
- The partial disposition of the balance recorded in API's OEB-approved Interim Distribution Licence Deferral Account from DLI customers
- The establishment of a new deferral account to record transaction and integration costs incurred by API, for recovery from all API customers after the acquisition, in lieu of a deferred rate rebasing period
- The classification of customers acquired by API in the DLI service area in accordance with API's existing rate classes upon the closing of the proposed transaction, after which they may be billed in accordance with API's approved Tariff of Rates and Charges
- The endorsement by the OEB of API's proposed approach to allocating costs attributable to the DLI service area to be used, at the time of API's next rebasing, primarily to API's R1 and R2 rate classes, which are eligible for Rural or Remote Rate Electricity Protection

OEB staff submits that, for the elements in which the "no harm" test can be applied, API's acquisition of the DLI distribution system meets the "no harm" test. Further, OEB staff submits that including a specific time period for compliance with OEB Code provisions is a reasonable approach for the requested licence condition but that any condition must be scoped to matters directly related to the management and operation of the existing DLI assets. OEB staff supports the proposed approach to most rates issues. While OEB staff is supportive of API's proposed cost allocation approach at a high level, OEB staff does not find that a blanket endorsement of API's proposed cost allocation methodology to be required or appropriate in light of the OEB's expectations for API's next cost of service application.

All of which is respectfully submitted.