EB-2018-0056

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sched. B, as amended;

AND IN THE MATTER OF an application by Niagara-on-the-Lake Hydro Inc. for an order or orders approving electricity distribution rates and other charges commencing as of May 1, 2019.

NIAGARA-ON-THE-LAKE HYDRO
2019 COST OF SERVICE RATES
REPLY ARGUMENT

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A. INTRODUCTION

1. On February 19, 2018, Niagara-on-the-Lake Hydro Inc. (NOTL Hydro) filed its Argument in Chief summarizing its proposals and evidence in respect of each of the six unsettled items. NOTL Hydro's Argument in Chief details why its proposals are reasonable and appropriate and should be accepted by the Ontario Energy Board (OEB, or the Board). As explained, NOTL Hydro's ratepayers are pleased with the service they receive, and approval of the utility's position will support NOTL Hydro continuing to provide safe, reliable, cost-effective service to its customers.

2. Three parties filed Arguments in response to NOTL Hydro – OEB Staff[1], School Energy Coalition (SEC)[2] and Vulnerable Energy Consumers Coalition (VECC)[3].

3. This Reply Argument sets out NOTL Hydro's response to the arguments advanced by the other parties in this proceeding. In addition to the items set out herein, NOTL Hydro repeats and relies on the positions taken and arguments set out in its Argument in Chief.

4. Before addressing the positions taken by other parties on the six unsettled issues in this proceeding, NOTL Hydro would like to address two high-level items that are included in the submissions from other parties. The unifying theme in these responses, and in NOTL Hydro's Application as a whole, is that NOTL Hydro has been even-handed and responsive to the expectations and needs of its ratepayers and the reasonable requests in this Application exemplify that commitment and approach.

5. The distribution rates to be paid by NOTL Hydro's customers is an important factor that underlies all of the unsettled items in this case. Ratepayers care about safe, reliable service at reasonable costs. NOTL Hydro's objective is to maintain low rates for its customers. As noted in Argument in Chief, NOTL Hydro's Mission Statement indicates (in part) that "Niagara-on-the-Lake Hydro continuously seeks to provide low cost energy delivery, high reliability and high power quality." This is a long-term objective, and NOTL Hydro has been successful in delivering on this goal, with significant progress achieved over time. The budgets and proposals included in NOTL Hydro's Application (including the remaining unsettled items)

[1] OEB Staff Submission on the Unsettled Issues, March 4, 2019 (OEB Staff Submission).
[2] Final Argument of the School Energy Coalition, March 4, 2019 (SEC Final Argument).
[3] Submission of the Vulnerable Energy Consumers Coalition, March 4, 2019 (VECC Submission).

further this goal. NOTL Hydro notes that, after adjusting for the ICM, the requested rate increase for its distribution rates is lower than would be received through an IRM.[4] If the OEB grants the relief requested by NOTL Hydro (see Section C of this Reply Argument), then its customers across its rate classes will continue to enjoy among the lowest rates in Niagara, and the province.[5]

6. OEB Staff and SEC give little credit to NOTL Hydro for its relatively low rates, focusing only on what they say is a recent trend showing that some of NOTL Hydro's costs have been increasing.[6] While it is true that some of NOTL Hydro's costs have increased in 2018, there are two key points to keep in mind. First, NOTL Hydro has maintained an overall positive trend of cost efficiency in recent years. A fair review of NOTL Hydro's performance looks at more than one year, and takes account of the fact that a small utility will have some "lumpiness" to its expenditure profile. NOTL Hydro's Additional Evidence on OM&A shows its PEG performance each year from 2014 to 2019[7] – it is clear that NOTL Hydro's cost performance continues to trend positively compared to expectations. This trend is what is important. Second, it should also be recognized that even if costs increase, rates can stay at a reasonable level. Where costs increase, but so too do customer numbers and load, then rates can remain reasonable.

7. The submissions from VECC and SEC question whether NOTL Hydro is preferring the interests of its shareholder (the Town of Niagara-on-the-Lake) over ratepayers.[8] This is unfounded and unfair. NOTL Hydro is directly focused on achieving safe, cost-effective, reliable service for its ratepayers. Ratepayers are not disadvantaged by NOTL Hydro's financing activities with the Town, since ratepayers actually pay less than the OEB's deemed cost of long-term debt for the utility's loans with the Town. Ratepayers are not disadvantaged by NOTL Hydro's practice of replacing overhead lines with underground lines in the "Old Town" and elsewhere. Ratepayers receive more reliable service and the character of their community is improved. And, of course, this is not a situation where the utility is owned by a private shareholder who is the beneficiary of the utility's decisions. NOTL Hydro's ratepayers

[4] Exhibit 4 – OM&A – Additional Evidence, page 5.
[5] Argument in Chief, paras. 18-23.
[6] Staff Submission, page 2; and SEC Final Argument, para. 15.
[7] Exhibit 4 – OM&A – Additional Evidence, page 7. Chart 6 from the Additional Evidence is reproduced below as Table 1.
[8] VECC Submission, para. 2.16; and SEC Final Argument, paras. 20, 21 and 30.

are also residents or business owners/operators in the Town. To the extent that utility activities benefit the Town and its residents, it does not necessarily follow that this will disadvantage ratepayers. NOTL Hydro operations are completely independent from those of the Town, NOTL Hydro does not rely on the Town for any services and the majority of the Board of NOTL Energy is independent of the Town.

B. ARGUMENT

8. Under the subheadings set out below, NOTL Hydro sets out its response to the arguments made by the other parties on each of the unsettled items.

a. Issue 1.1 – Capital Expenditures – Underground Conversion Program

9. As set out in the Settlement Proposal, most of NOTL Hydro's proposed capital expenditures for 2019 have been resolved (and now approved), along with most of the rate base impact of capital expenditures for the 2014 to 2018 incentive regulation (IR) term.[9]

10. The outstanding issue relates to the costs of NOTL Hydro's underground voltage conversion project/program, both in relation to amounts spent since the 2014 rebasing (impacting 2019 opening rate base) and to the proposed Test Year expenditures (impacting 2019 net additions and rate base).

11. As explained in Argument in Chief, NOTL Hydro's underground voltage conversion program is appropriate and necessary, and it is being implemented in a measured and reasonable manner.[10]

12. VECC devotes a lot of attention to NOTL Hydro's 2014 cost of service proceeding (EB-2013-0155), and asserts that the utility may have misled the OEB about the municipal imperative for the underground program, as well as about how long it would take to complete the program.[11] NOTL Hydro takes strong exception to these accusations. There is no evidence that NOTL Hydro provided anything but the best information available at the time in the prior

[9] Exhibit N1, Tab 1, Schedule 1, Settlement Proposal, January 10, 2019, at Items 1 and 2, pages 9 to 12.
[10] Argument in Chief, paras. 27-39.
[11] VECC asserts that its agreement to the 2014 cost of service case settlement on the underground conversion program was premised on an understanding that the utility was compelled by the municipality to do the underground work. However, there is no evidence as to what led each party to the 2014 Settlement Agreement. NOTL Hydro's interrogatory response reproduced in the VECC Submission indicates that NOTL Hydro has been "burying facilities in the Old Town because … it is the right thing to do". See VECC Submission, para. 2.1.

cost of service proceeding. NOTL Hydro's evidence in the prior case, and in this case, is that underground installation of replacement facilities is the right thing to do in many parts of the Town. That is the case whether or not a by-law is in place, and NOTL Hydro does not assert it would act differently in respect of the underground voltage conversion program if there was no by-law in place.

13. In the 2014 cost of service case, NOTL Hydro pointed to its interpretation of existing by-laws requiring underground installation of new facilities in the "Old Town", but also acknowledged that the by-laws might not restrict its ability to install new overhead facilities. NOTL Hydro explained that regardless of what by-laws might require, it chooses to use underground installation in the "Old Town" because that is "the right thing to do". This is seen in the interrogatory response reproduced by VECC in its submission. It is also seen in a response to a Board Staff Interrogatory in that same proceeding, where NOTL Hydro indicated that:

> *NOTL Hydro is cognizant of the fact that a Town by-law may not restrict our ability to install new overhead facilities in the Old Town. However, we choose to bury facilities in the Old Town because we believe it is the right thing to do. This 'underground' practice commenced over 25 years ago with the Niagara-on-the-Lake Hydro Commission and has continued with NOTL Hydro. Our previous rate applications and Conditions of Service also clearly outline(d) our plans to bury facilities in the Old Town. Customers living in the Old Town have for over 25 years been required to pay the additional cost of burying their supply cables to their homes when modifying their service. Customers have willingly accepted this additional cost and we have never had a related dispute.*[12]

14. NOTL Hydro's Distribution System Plan filed in the 2014 cost of service application indicated that "[w]e estimate that the entire historic Old Town will be converted to 27.6 kV and buried within 15 years."[13] The map filed by NOTL Hydro in its submission in 2014 also showed conversion work in the Old Town going out to 2026.[14] NOTL Hydro filed an interrogatory response in that proceeding indicating that it was "confident" the work in "Old Town" could be completed by 2022.[15] The various timeframe estimates may not have been consistent but they all point to a long-term project.

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[12] EB-2013-0155 NOTL Hydro 2014 COS Application, responses to Board Staff Interrogatories, Response to 5.1-Staff-12(b), found at: http://www.rds.oeb.ca/HPECMWebDrawer/Record/424731/File/document (at page 28 of 98).
[13] EB-2013-0155 NOTL Hydro 2014 COS Application, Consolidated Distribution System Plan (page 84), found at: http://www.rds.oeb.ca/HPECMWebDrawer/Record/411394/File/document.
[14] EB-2013-0155 NOTL Hydro 2014 COS Application, Distribution System Plan, Attachment 16, Capital Plan Maps.
[15] See interrogatory response reproduced at paragraph 2.1 of the VECC Submission.

15. There is nothing to suggest that the information provided by NOTL Hydro in the 2014 cost of service proceeding was anything except NOTL Hydro's best information at the time. As explained in evidence in this case, it has subsequently become apparent that the underground conversion program will take longer than anticipated, based on more current information.[16] Importantly, as the pace of the underground conversion program slowed over the past 5 years, the spending also went down to a level well below the amounts that had been forecast.[17]

16. The context set out above explains why NOTL Hydro strongly contests VECC's suggestion that NOTL Hydro has previously misled the regulator. Coming to that conclusion would require evidence that NOTL Hydro knowingly provided incorrect information. There is no such evidence. It is significant that neither of the other parties in this proceeding make any similar accusation.

17. There should be no issue in this case as to the prudence of amounts already spent on NOTL Hydro's underground conversion program. The expenditures were prudent, and were within the scale, scope and type reviewed and accepted in the EB-2013-0155 cost of service proceeding (for 2014 rates). Neither OEB Staff nor SEC make any argument for a disallowance of including completed underground conversion projects in rate base. VECC's position in this regard is not based on the prudence of any specific completed projects or expenditures. VECC does not explain what disallowance would be appropriate, nor on what basis. NOTL Hydro therefore submits that its proposed opening rate base (inclusive of underground conversion program projects) should be approved as filed.

18. The common issue among all the parties in this case is whether the full amount of NOTL Hydro's proposed 2019 Test Year expenditure for the underground conversion program should be approved. Each of Board Staff and SEC argue for a reduction of the proposed budget, based on past underspending.[18] VECC asserts that the OEB should require a more searching review of the entire underground conversion program in the next cost of service application and permit underground conversion only in the "Old Town" area in the interim.[19]

[16] Exhibit 2 – Additional Evidence – Underground Voltage Conversion, page 8.
[17] This can be seen in Table 1 of the Board Staff Submission, at page 5.
[18] Board Staff Submission, pages 5-7; and SEC Final Argument, para. 9.
[19] VECC Submission, para. 1.3.

19. NOTL Hydro has explained why its entire proposed budget for its underground conversion program and general underground work is appropriate and necessary.[20]

20. The fact that less has been spent in recent years than had been forecast does not mean that this trend will continue during the next IR term. NOTL Hydro expects that the entire budgeted amount is needed and will be spent.

21. To the extent that the OEB believes that a reduction to the proposed underground conversion program budget is appropriate based on prior actual spending, then NOTL Hydro believes that it is appropriate for the OEB to properly identify what has been the recent actual spending relative to forecast amounts. The OEB Staff Submission concludes that NOTL Hydro underspent by around 28% per year, once the impact of capitalized management time is taken into account.[21] If applied to NOTL Hydro's $340,000 Test Year underground conversion budget at issue in this case, this would translate to a $95,000 reduction.

22. NOTL Hydro questions whether any reduction to this budget is warranted, given that there are clear plans for underground conversion work throughout the upcoming IR term, However, if the Board does believe that reduction is necessary, the detailed approach in the OEB Staff Submission to determine an applicable reduction is more appropriate than the high-level estimate included in the SEC Final Argument.

23. There is one final item related to this unsettled issue to which NOTL Hydro would like to respond,

24. In their submissions, the other parties each take different views about the customer engagement conducted on NOTL Hydro's underground conversion program. OEB Staff note that NOTL Hydro's customers do not appear to oppose the program.[22] SEC indicates that it is not clear if the level of spending takes customers' views into account.[23] VECC states that there has not been sufficient consultation on the costs and benefits of the underground conversion program.[24]

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[20] See Argument in Chief, para. 38 (and associated references). The plans and associated costs are also addressed in NOTL Hydro's Distribution System Plan (filed at Exhibit 3 – for example, see pages 55-58).
[21] Board Staff Submission, pages 5-7.
[22] Board Staff Submission, page 4.
[23] SEC Final Argument, paras. 7-8.
[24] VECC Submission, paras. 2.14 -2.16.

25. In NOTL Hydro's view, the suggestion that deeper consultation was required is an attempt to create an issue where none exists. NOTL Hydro is a small utility and is in close contact with its customers. NOTL Hydro is aware of and responsive to concerns and questions raised by customers. Customers are not complaining about their rates in general, or about the underground conversion program in particular. This is not a new program that the utility is now considering. It is a long-standing program (over 30 years) that has not attracted complaints and concerns. Additional customer engagement should not be expected to change this.

b. <u>Issue 1.2 – OM&A Expenditures</u>

26. As explained in Argument in Chief, NOTL Hydro's 2019 Test Year OM&A forecast is \$2,964,765.[25] This is the amount required for NOTL Hydro to continue its safe, reliable and customer-focused operations. Included in NOTL Hydro's OM&A operating costs are required expenditures necessary to maintain and operate NOTL Hydro's distribution system and transmission station assets, the costs associated with metering, billing, collecting from its customers, the costs associated with ensuring all stakeholders' safety (public and employees) and costs to maintain the distribution business service quality and reliability standards set by the regulating bodies.[26]

27. NOTL Hydro's Argument in Chief details several analyses that confirm the reasonableness of NOTL Hydro's 2019 OM&A budget forecast including: (i) the elements of the budget; (ii) comparing the budget to the most recent actual spending; (iii) the details and appropriateness of the various year-over-year cost increases between the last rebasing and 2019; (iv) expected increase in the budget from the last rebasing; and (v) comparing NOTL Hydro's OM&A per customer to other distributors.[27]

28. The other parties in this proceeding each propose that NOTL Hydro's 2019 OM&A budget should be reduced. Different budget levels and rationale are included by each party.

29. What is common to each of the arguments presented by other parties is an approach that starts with NOTL Hydro's 2014 Board-approved OM&A budget and then adjusts that number

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[25] Argument in Chief, para. 40.
[26] Exhibit 4 – OM&A, page 4.
[27] Argument in Chief, paras. 43-62.

based on inflation, stretch factor and other items.[28] None of the arguments look at the details of any of the proposed OM&A expenditures. Importantly, no objections are raised as to the programs and staff that NOTL Hydro proposes to employ in the coming years. That makes concerns about the overall budget ring somewhat hollow.

30. NOTL Hydro submits that there are several problems with the approach taken by each of the other parties. Therefore, the evaluation approach used by NOTL Hydro in its Argument in Chief should be preferred to the approaches employed by other parties. If the OEB decides to use the approach proposed by any of the other parties, then adjustments should be made to address/correct the issues discussed below.

31. First, contrary to the position taken by OEB Staff[29] and VECC[30], it is entirely appropriate for NOTL Hydro to include the cost of previously capitalized employee expenses in the OM&A budget forecast for 2019.

    i. As detailed in Argument in Chief, during 2014 NOTL Hydro's President and the VP Operations booked time to capital, as appropriate under Canadian GAAP, while in 2019 this will be limited, because IFRS rules are now being applied. The reduction in capitalized costs, and corresponding addition to OM&A costs, is $130,784.41.[31] These are not new costs that the utility should be expected to absorb within an inflation-adjusted budget. They are recategorized costs that are no longer being booked as capital expenses (with a corresponding savings because ratebase impact is reduced).

    ii. Even assuming that OEB Staff is correct that NOTL Hydro should have expensed these costs as part of its 2014 cost of service filing, that does not mean that ratepayers have been harmed. NOTL Hydro has only ever reflected these costs in one place (initially as capitalized expenses and later as OM&A costs). All parties accepted NOTL Hydro's 2014 capital budget forecast, which included these costs. Ratepayers would

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[28] As stated in Argument in Chief (para. 49 and footnote 33), an approach that compares the 2019 Test Year OM&A forecast with the budget from the last cost of service year should use NOTL Hydro's 2014 actual OM&A expenditures as a starting point because they represent the actual costs of the relevant year. NOTL Hydro's 2014 actual 2014 OM&A expenditures were around $55,000 higher than the compromise Settlement Proposal budget amount cited by each of the other parties.
[29] OEB Staff Submission, pages 13-14.
[30] The VECC Submission does discuss this discrete expense item.
[31] Argument in Chief, para. 54.

receive a windfall, and the utility would be penalized, if NOTL Hydro is not now permitted to recover these costs within OM&A expenditures.

iii. SEC agrees with NOTL Hydro that the capitalized employee expenses should be included in the 2014 OM&A base amount used to assess 2019 OM&A budget.[32] The point of using an earlier budget to assess a new forecast is to make an “apples to apples” comparison. To do that, the same items should be included in both budgets. The 2019 budget forecast includes the previously capitalized costs noted above – to fairly compare the current budget to the earlier budget requires that these costs be imputed into the prior budget.

32. Second, the adjustment factors used by SEC and VECC in their analyses are understated.

i. NOTL Hydro notes that OEB Staff appears to accept the adjustment factor approach applied by NOTL Hydro (using both customer and load growth as factors influencing expected OM&A costs).[33]

ii. SEC cites the approach taken by the OEB in a recent case which adjusted the prior Board-approved budget by inflation and customer growth with an offset for a stretch factor, and applies a proposed adjustment approach that results in a lower number than NOTL Hydro’s 2019 OM&A forecast.[34] NOTL Hydro believes that this approach improperly excludes the impact of load growth, which is a significant driver of OM&A costs, especially for a distributor like NOTL Hydro that has transmission assets.[35]

iii. NOTL Hydro notes that in a recent case where the OEB used a formulaic approach to evaluate Test Year OM&A as compared to prior Board-approved budgets, the OEB also allowed for additional extraordinary expenses to be added to the amount derived using a formula.[36] NOTL Hydro has provided evidence and argument about the extraordinary cost pressures that it faces that are not accommodated in a budget that

[32] SEC Final Argument, paras. 13(ii) and 18.
[33] OEB Staff Submission, page 9 (footnote 27) and page 10 (where OEB Staff object to including the previously capitalized labour in the 2014 OM&A base amount, but do not object to NOTL Hydro’s adjustment approach).
[34] SEC Final Argument, paras. 13(i) and 18.
[35] Exhibit 4 – OM&A – Additional Evidence, pages 2 and 8.
[36] See EB-2016-0085 Innpower Corporation, Decision and Order dated March 8, 2018 (at pages 23-25).

simply increases for inflation and growth. These items should be reflected in NOTL Hydro's 2019 Board-approved OM&A budget.

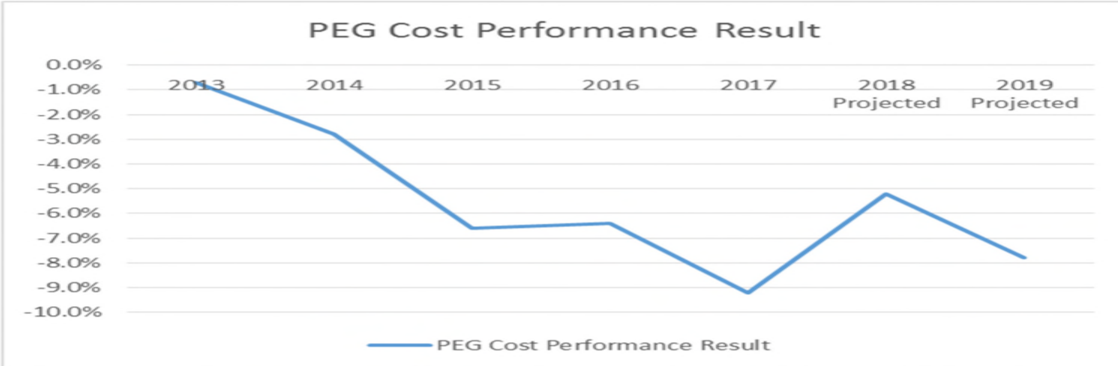
iv. VECC takes a higher-level approach of applying inflation and customer growth to derive a proposed 2019 OM&A budget. It is not entirely clear how its adjustment factors were derived.[37] It is also not clear whether VECC has compounded or combined the effect of the factors it used (which would be appropriate). What is clear is that VECC has not included any impact for load growth, nor any allowance for extraordinary cost pressures.

33. Another common theme in the submissions from other parties is the assertion that NOTL Hydro's OM&A costs per customer are trending negatively, and this supports reducing the proposed Test Year OM&A budget forecast.[38] NOTL Hydro disagrees. As seen in Table 7 of NOTL Hydro's Argument in Chief, the utility's operating cost per customer was virtually the same as the industry average in the last year for which actual data was available. Indeed, NOTL Hydro's actual OM&A cost per customer has never been significantly different from the industry average during any year since 2010. That is a good achievement for a utility that has relatively low customer density[39], and uses 30% of its assets for transmission purposes.[40]

34. NOTL Hydro's actual cost performance is improving when evaluated through the lens of the PEG benchmarking analysis. NOTL Hydro has maintained its ranking within cohort 3 (where its costs are within the expected range[41]) throughout the current IR term. In each year, NOTL Hydro's cost performance has been better than what would be expected. NOTL Hydro's performance has been improving over time (trending positively), using the evaluation method employed by PEG, as seen in Table 1 below, reproduced from NOTL Hydro's Additional Evidence[42]:

[37] VECC Submission, paras. 3.3 and 3.4.
[38] See VECC Submission, para. 3.7; SEC Final Argument, para. 14; and OEB Staff Submission, pages 10-11.
[39] Exhibit 4 – OM&A – Additional Evidence, pages 3-4.
[40] Exhibit 4 – OM&A – Additional Evidence, pages 2 and 8.
[41] Pacific Economics Group (PEG) Report to the Ontario Energy Board titled "Empirical Research in Support of Incentive Rate-Setting: 2017 Benchmarking Update", pages 8-9. PEG Report filed at https://www.oeb.ca/sites/default/files/PEG-benchmarking-report-20180823-revised.pdf
[42] Exhibit 4 – OM&A – Additional Evidence, page 7.

Table 1 – NOTL Hydro PEG Performance



35. NOTL Hydro's evidence is that based on the trends of its costs, it may be able to achieve a rating within cohort 2 of PEG's rankings, which is the group with actual costs more than 10% lower than the expected costs in the not too distant future. Contrary to the submissions of other parties, this demonstrates reasonable performance, and it demonstrates continuous improvement and positive outcomes for ratepayers. None of this is a basis for penalizing NOTL Hydro and reducing its forecast OM&A budget forecast for 2019.

36. VECC submits that reductions to NOTL Hydro's 2019 OM&A budget forecast should be made in recognition of the alleged excessive spending on the underground conversion (capital) program.[43] No specific suggestion is made as to what reduction is appropriate. In response, NOTL Hydro asserts that there is no basis for this proposed adjustment. It has not been established that NOTL Hydro's historic spending on the underground conversion program is "excessive". The spending on that program during the 2014 to 2018 IR term has been lower than forecast and endorsed in the 2014 cost of service proceeding.[44] The activities undertaken were reasonable and appropriate. The approach suggested by VECC amounts to punishment (they call it "rough justice"[45]) for a non-existent crime.

37. As explained in Argument in Chief, a key way to evaluate NOTL Hydro's Test Year OM&A budget forecast is to look at the most recent actual expenditures. The utility is incented to keep OM&A expenditures as low as possible during an IR term, because lower spending directly translates into higher returns for its shareholder. Therefore, actual spending shows what the utility really needs to provide safe, reliable, responsive, cost-effective service to its

[43] VECC Submission, para. 3.9.
[44] This can be seen in Table 1 of the Board Staff Submission, at page 5.
[45] VECC Submission, para. 2.24.

customers. A reduction from OM&A amounts already being spent will cause NOTL Hydro to have to choose between current activities and programs, and reduce services that benefit customers.

38. The OEB agreed in a recent case that looking at the most recent actual OM&A expenditures and adjusting for inflation, growth and stretch factor is an appropriate way to evaluate the forecast Test Year budget.[46] Applying this approach to NOTL Hydro's application results in a forecast 2019 OM&A budget that is very close to the as-filed budget.

39. NOTL Hydro's best evidence of its actual 2018 OM&A expenditures is $2,838,525.[47] That should be the starting point for adjustments to determine a 2019 budget level. As set out in Table 5 of NOTL Hydro's Argument in Chief, the combination of inflation, growth factors and stretch factor from 2018 to 2019 equates to an increase of 3.71%. Applying that escalation factor to 2018 actuals results in a 2019 OM&A budget forecast of $2,943,834. This is very close to NOTL Hydro's filed 2019 OM&A budget forecast of $2,964,765. Even if one was to simply apply an adjustment of 1.7% based on the OEB's 2019 inflation factor to the 2018 actuals, this would result in a 2019 OM&A budget forecast of $2,886,780, which is also close to the as-filed 2019 budget forecast. It is important to highlight that an approved OM&A below the 2018 base spending adjusted to 2019 will not support NOTL Hydro's current and planned operations for 2019[48], and will result in important and beneficial programs and activities being reduced or not pursued.

40. For the reasons described in Argument in Chief, and taking into account NOTL Hydro's response to the positions advanced by other parties, NOTL Hydro repeats its request that the OEB approve the as-filed 2019 OM&A budget forecast. This will support continued safe, reliable and responsive service to NOTL Hydro's customers.

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[46] EB-2016-0105, Thunder Bay Hydro Electricity Distribution Inc., Decision and Order dated September 21, 2017 (page 5).
[47] SEC suggests that the increase from 2017 to 2018 is unduly high – this argument fails to recognize that a big part of the increase (around $100,000) results from moving costs for the President and VP-Operations from capital to OM&A – these are not new costs in 2018, they are recategorized costs (see 4-SEC-42 and 4-VECC-29).
[48] New expenditures currently planned for NOTL Hydro in 2019 include Cybersecurity and the Utilismart initiative which would provide large customers with better access to their data.

c. <u>Issues 2.1 and 2.2 – Cost of Long Term Debt</u>

41. NOTL Hydro's long-term debt consists of six debt instruments, three from third parties (CIBC and Infrastructure Ontario) and three from the Town of Niagara-on-the-Lake.[49] NOTL Hydro's overall proposed cost rate for long-term debt for 2019 is 3.95%, which is lower than the OEB's deemed cost of long-term debt for 2019 (which is 4.13%).[50]

42. The outstanding issues related to NOTL Hydro's long-term debt relate to the three debt instruments from the Town (two demand loans and a promissory note). NOTL Hydro's Additional Evidence explains the benefits of its loans from the Town, as compared to loans from a financial institution.[51] These loans do not include financial covenants and the loans are unsecured. These are important to NOTL Hydro as this means its borrowing capacity with financial institutions is not affected. As a small company, NOTL Hydro believes it is very important to maintain this financing flexibility so that if new debt is needed, as will be the case in 2019 with the new transformer, it can be obtained on favourable terms.[52] NOTL Hydro's very low debt to equity ratio is further evidence of this.[53]

43. OEB Staff supports NOTL Hydro's proposed 2019 cost of long-term debt.[54]

44. SEC is the only party to take issue with the debt rate associated with NOTL Hydro's promissory note with the Town. While the actual interest rate associated with that loan is 7.25%, for ratemaking purposes NOTL Hydro is including the instrument at the OEB's deemed rate for long-term debt (4.13%). Ratepayers are not paying for any amount over the OEB's deemed rate.

45. SEC argues that ratepayers should only pay a current rate for the promissory note, and asserts that is lower than the OEB's deemed rate.[55] NOTL Hydro strongly disagrees with that position. As explained, NOTL Hydro and its ratepayers benefit from the utility getting some of its debt from its shareholder. That supports some premium over market rates. Moreover, the OEB has specifically contemplated the scenario where a utility obtains debt from an

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[49] Argument in Chief, para. 66 (and associated references).
[50] Argument in Chief, para. 68.
[51] Exhibit 5 – Additional Evidence – Cost of Long-term Debt, page 2.
[52] Argument in Chief, para. 70 (and associated references).
[53] Exhibit 1 – Administration, page 49.
[54] OEB Staff Submission, pages 16-18.
[55] SEC Final Argument, para. 24.

affiliate with a cost rate in excess of the OEB's deemed rate. In that circumstance, the OEB requires the utility to recognize the debt at the deemed rate for ratemaking purposes. This is what NOTL Hydro has done in the past, and continues to do now.[56] There is no need to further "balance" interests of ratepayers and shareholders.

46. As explained in Argument in Chief, the Town has required that NOTL Hydro's two demand loans be replaced with new loans at current interest rates (3.5%), effective on March 1, 2019. NOTL Hydro is valuing the two demand loans at their actual cost (3.5%), which is lower than the OEB's 2019 deemed rate for long-term debt, and it is valuing the promissory note at the OEB's 2019 deemed rate (4.13%). This means that ratepayers are not harmed, and are actually in a better position than if the utility simply used the OEB's deemed cost of long-term debt for all of its debt.[57]

47. VECC is not correct when it states that there is no apparent reason for the change in debt rates.[58] As explained in a letter from the Town to NOTL Hydro that is reproduced in the evidence, the reason for the increase is that the Town wishes to receive market rates for its demand loans.[59] That is not unreasonable.

48. VECC also seems to want "proof" that the updated loans will actually be put in place.[60] NOTL Hydro believes that the evidence that it has provided on the subject is sufficient. However, in case it is helpful NOTL Hydro can advise that on March 4, 2019, the Town approved proceeding with the new demand loans with interest rates of 3.5%, effective as of March 1, 2019.[61]

49. SEC takes issue with the fact that NOTL Hydro has not required formal notice from the Town about the renegotiation of the demand loans, and therefore the 45 or 90 day notice period leading up to the effective date for new loans should not be deemed to have started.[62] That position puts form over substance. As seen in the letter from the Town to NOTL Hydro dated

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[56] Argument in Chief, para. 72 (and associated references).
[57] Argument in Chief, paras. 73-74.
[58] VECC Submission, para. 4.4.
[59] Exhibit 5 – Additional Evidence – Cost of Long-term Debt, page 2. As described, the discussions around increasing the interest rate started before the ADR session in this case and continued after that time.
[60] VECC Submission, para. 4.6.
[61] See Minutes of March 4, 2019 meeting, found at: http://cotw.notl.org//sites/notl/NOTLCOTW.nsf/74C6E02BCBF6FC1C8525783E00620D4E/18BBBCA94843A41E85258399004CEDB4
[62] SEC Final Argument, paras. 29-30.

December 19, 2018 (which was preceded by discussions in November 2018), the Town has made it abundantly clear that it intends to re-set the interest rates associated with the demand loans.[63] These discussions (including the written letter) took place more than 90 days before the effective date of the new loans.

50. Finally, NOTL Hydro does not agree that the updated rates associated with the demand loans should be pro-rated to reflect only the period when the new rates should be in effect during the 2019 calendar year.[64] The updated rates (and associated costs) will be in place throughout this IR term and are properly included in the base long-term debt costs.[65]

d. <u>Issue 3.2 Cost Allocation: Inclusion of ICM Revenues in Existing Rates</u>

51. NOTL Hydro's filing calculated proposed 2019 rates by including Incremental Capital Module (ICM) revenue in distribution revenue at current rates in the cost allocation model.

52. As explained in Argument in Chief[66], NOTL Hydro believes this is an appropriate approach in the circumstances of this case. The ICM revenues relate to a new transformer asset. The costs for that asset will continue to be recovered from customers from 2019 and beyond. The only difference will be that from and after 2019, revenues associated with the ICM asset will be recovered through rates rather than through a rate rider.

53. VECC supports NOTL Hydro's proposal.[67] The other two parties assert that the OEB should continue with its *status quo* approach, and require NOTL Hydro to exclude ICM revenues from revenues at existing rates.[68]

54. NOTL Hydro acknowledges that its approach is different from what has been done by other distributors in their first rebasing following an ICM. However, that does not mean that the proposed approach is unreasonable or inappropriate. In fact, each of the other parties have acknowledged that NOTL Hydro's proposal is reasonable – OEB Staff states that this "could

[63] Exhibit 5 – Additional Evidence – Cost of Long-term Debt, page 2.
[64] SEC Final Argument, para. 28.
[65] If the OEB were to choose to take this approach, then the proper way to proceed is to treat the new rates as being in place for 9 of 12 months, meaning that the effective rate associated with the demand loans is 3.375% (equal to (3%*3 months plus 3.5%*9 months, divided by 12).
[66] Argument in Chief, paras. 75-79.
[67] VECC Submission, paras. 5.10 - 5.11.
[68] OEB Staff Submission, page 21, and SEC Final Argument, para. 39.

be seen as a reasonable proposal"[69]; SEC states that NOTL Hydro's "rationale for including the ICM rate rider in revenue in existing rates has merit and is reasonable"[70]; and VECC states that "the approach adopted by NOTL is appropriate and should be accepted by the Board .."[71].

55. NOTL Hydro submits that consistency with previous applications is not sufficient reason to deny its proposal. There are valid reasons why a departure from the OEB's historic approach is appropriate. As explained by VECC, "the revenues at *status quo* rates are meant to reflect the situation that would occur if all customer classes receive the same percentage rate increase [and] Since all customers are currently paying the ICM rate rider as part of the "cost" of their distribution service it is logical that the revenues [would] be included."[72]

56. This is not a situation where a distributor is unduly favouring one customer class over another. NOTL Hydro's proposed approach seeks consistency between the existing situation (where customers are paying distribution rates plus ICM) and the future situation (where the ICM costs will be included in the distribution rates). The positive impact of NOTL Hydro's approach for some customers (lower residential rates) should not raise concern because of the fact that the corresponding negative impact (higher rates for GS>50kw customers) will be felt by a customer class that currently has among the lowest rates in Ontario.[73]

e. <u>Issue 4.2 DVAs: Disposition period of Group 2 DVAs and LRAMVA</u>

57. As explained in Argument in Chief, NOTL Hydro believes its customers would benefit from, and prefer, having the impact of the Group 2 deferral and variance accounts (Group 2 DVAs) and LRAM rate riders spread over two years rather than just one year.[74] This is consistent with the approach that has been employed by NOTL Hydro in the past for accounts with relatively large balances.[75] NOTL Hydro's proposal also takes account of the fact that customers were not told of the relatively large rate riders during the customer consultations, because at that time there was an error in the model that led NOTL Hydro to believe that the rate riders would be modest.

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[69] OEB Staff Submission, page 21.
[70] SEC Final Argument, para. 38.
[71] VECC Submission, para. 5.10.
[72] VECC Submission, para. 5.11.
[73] Exhibit 4 – OM&A – Additional Evidence, page 2.
[74] Argument in Chief, paras. 80-84.
[75] Exhibit 9 – Additional Evidence – Deferral and Variance Accounts – Group 2 and LRAM Rate Riders, page 2.

58. No party strongly opposes NOTL Hydro's proposal. While parties note that the impact of the Group 2 DVA and LRAM rate riders will be less than 10% (the usual threshold for mitigation measures), they do acknowledge that a two year clearance may be appropriate in this case.

59. OEB Staff supports the two-year disposition period, to manage bill impacts and customer expectations. OEB Staff indicates that the $5,000 in additional interest costs that will be borne by customers over the extended disposition period is not significant, given the value provided to customers by managing bill impacts.[76]

60. VECC does not express a firm view, but does acknowledge that a two-year disposition period may be appropriate because it will support more consistent bill increases in the coming years.[77]

61. SEC indicates that customers would prefer to pay the Group 2 and LRAM rate riders over one year, rather than pay interest on uncleared amounts. SEC does allow that NOTL Hydro's proposal could be accepted if NOTL Hydro is prepared to forego the collection of the additional interest on the second year's balance.

62. NOTL Hydro continues to believe that its customers prefer and would benefit from clearance of the Group 2 and LRAM rate riders over two years. To ensure that its customers will receive this benefit, NOTL Hydro is prepared to forego the additional interest that would accrue on the uncollected balance of these accounts over the two years. This could be accomplished by reducing the principal balance to be recovered by $5,000. NOTL Hydro submits that this proposed approach is in the interest of ratepayers, and should be approved.

f. Issue 5.3 Transmission Gross Load Billing

63. NOTL Hydro has applied to have the Retail Transmission Rate – Line and Transformation Connection Service Rates for Load Displacement Generators (LDG), with a generator unit rating of 2 MW or higher for renewable generation and 1 MW or higher for non-renewable generation applied on a gross load billing basis consistent with the method charged for Line and Transformation Connection Services by the IESO. As explained, without gross billing of Retail Transmission Rate - Line and Transformation Connection, NOTL Hydro's other

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[76] OEB Staff Submission, pages 22-23.
[77] VECC Submission, para. 6.8.

customers will be subsidizing the gross load billing transmission costs for any future LDG customers.[78]

64. No party objects to NOTL Hydro's proposal on any principled basis. Both SEC and VECC agree that there is merit in aligning NOTL Hydro's billing of customers with the way that NOTL Hydro is billed by the IESO.[79] This is different from the Erie-Thames Powerlines Corporation proceeding where a party to be impacted by transmission gross load billing was an active participant.[80]

65. The only concern raised is around whether the OEB plans to look at transmission gross load billing on a generic basis, and whether any change to NOTL Hydro's rates should await that process.[81] NOTL Hydro submits that this is not adequate reason to refrain from approving the proposal. It is not appropriate for NOTL Hydro's other customers to pay costs caused by a Large User where such costs can be directed to the Large User. The fact that NOTL Hydro has not applied this transmission gross load billing before now is simply a reflection of the fact that there has been no customer causing upstream gross load billing costs. Contrary to the OEB Staff Submission[82], that should not prevent the OEB from approving such a charge now. NOTL Hydro submits that approving its current proposal will not impair the OEB's ability to look at the question of transmission gross load billing on a generic basis at a later time. If the OEB directs an approach that is different from what is in place for NOTL Hydro, then NOTL Hydro can implement that different approach at that time.

C. REQUESTED RELIEF

66. In summary, NOTL Hydro respectfully requests OEB approval of the following items:

   i. The as-filed cost of the underground capital expenditures for 2019, and the inclusion into rate base of all amounts spent on the underground conversion program during the 2014 to 2018 term;

   ii. The as-filed OM&A budget for 2019;

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[78] Argument in Chief, paras. 85-90.
[79] SEC Final Argument, para. 43; and VECC Submission, para. 7.3.
[80] EB-2017-0038 Erie Thames Powerlines Corporation, 2018 Cost of Service Application – see August 1, 2018 Notice of Appeal from Toyota Motor Manufacturing Inc. which set out the topics of interest to that party.
[81] OEB Staff Submission, pages 24-25; and SEC Final Argument, para. 43.
[82] OEB Staff Submission, page 25.

iii. The as-filed updated cost of long-term debt for 2019;

iv. The determination of 2019 rates using a cost allocation approach that includes 2018 ICM revenues in revenue at existing rates;

v. The clearance of Group 2 Deferral and Variance Accounts and the LRAMVA over two years, with a reduction of $5,000 to the principal balance being recovered (to reflect the difference in interest costs); and

vi. The proposed transmission standby charge for the Large User rate class.

All of which is respectfully submitted this 15th day of March 2019.

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