North Bay (Espanola) Acquisition Inc.
EB-2019-0015
Procedural Order No. 4
Donald D. Rennick Submissions
June 28, 2019

Preamble

1. In order to be a true "no harm" test, the status quo must be compared to the results following the taking of any action. In this application the financial status quo of hydro customers must be compared to their circumstances after completing any amalgamation. It appears that the emphasis in the application was to embellish benefits as opposed to providing evidence of no harm.

Final Recommendation

2. It is submitted that the Applicant did not meet the "no harm" test and the amalgamation does not meet the Board's statutory objectives particularly in regards to price. The following is evidence of the negative effects of amalgamation and a discussion of the discerned benefits.

Submissions

3. The Applicant's arguments describe the unique aspects of the application[1] to support the requested rate framework proposal and the regulatory issues facing ERHDC. It is possible that correction of any deficiencies may provide a benefit to ERHDC. However, it is not the mandate of the Applicant to come to the rescue of ERHDC regardless of any perceived issues. From a business perspective, there would be no incentive in either of these issues that would induce the customers of NBHDL to consider an amalgamation with ERDHC. These arguments are a non-issue in suggesting no harm.

4. The Applicant submits that the sharing of expertise following the amalgamation will result in a higher quality of operations that will benefit <u>both</u> the customers of NBHDL and ERHDC [2]. The Applicants response to a request for further clarification [3] did not offer any evidence that the remark was anything other than promotional rhetoric. There appears to be no benefit accruing to the customers of NBHDL in the sharing of expertise with ERHDC.

[1] Application - Page 2
[2] Ibid - Page 16 – Line 13
[3] IRR – Page 39 – Line 8 and Response to Donald D. Rennick Submissions – DDR-1 (b) – Page 5

5. The Applicant details the OEB's desire to encourage amalgamations [4] and reduce the number of individual LDC's operating in Ontario. This issue is a direct result of government actions. It appears that being faced with the workload and expense resulting from creating what once amounted to over 140 LDC's that hydro customers are being asked to pay to alleviate the bureaucratic burden that this action produced.

6. While the amalgamation advances the OEB agenda it provides no reasonable incentive to the customers of NBHDL. This is especially true when it is clear from the evidence that NBHDL customers will not benefit from any savings resulting from the amalgamation of administrative functions of the two operations. Table 7-1 in the application illustrates that the OM&A costs per NBHDL customer will be unchanged whether or not the amalgamation takes place. Cost per NBHDL customer with no amalgamation in 2026 is $8,624/24,117 or $358. If amalgamation occurs, NBHDL cost per customer in 2026 is 88%*($9,781/24,117) or $357 [5]. The Applicant is misstating the facts by suggesting overall costs will be lower to service a larger customer base [6]. Table 7 – 1 clearly indicates there is an increase in overall costs from - $8,791 in 2019 to $9,781 in 2026.

7. Tax liabilities associated with the forecasted savings will amount to 21% at current rates and have not been considered. Since any savings will increase taxable income, the tax liability will range from $120,000 to $145,000 per year and would reduce actual savings. As indicated above, the lower per customer cost will benefit ERHDC customers only.

8. The Applicant submits that there will be no impact with respect to price or underlying costs following Phase 1 [7]. The facts are that the new ERHDC will experience an increase in underlying costs resulting from the principal and interest payments required to service the approximately $8 million purchase price loan [8]. These are additional costs and the funds required, amounting to approximately $1.2 million [9] over three years until 2022, must necessarily be collected from customers or obtained from the funds now being collected and diverted from the needs that those funds are presently servicing. These additional costs represent harm to customers when compared to the status quo.

9. Following Phase 2 and the amalgamation of ERDHC and NBHDL, the new NBHDL will be liable for the principal and interest payments to outside lenders on the balance of

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[4] Argument – Page 4 – Line 14
[5] DDR IR - Schedule A - Page 3
[6] IRR – Page 49 - Line 18
[7] Argument – Page 7 - 30(b)
[8] Application – Page 37 – Line 7
[9] Purchase Price – Amortization Schedule.xlsx

the $8 million loan. These are additional payments and the funds required, amounting to approximately $9.5 million [10] over the next 25 years, will be in addition to current costs. Given the current customer ratios[11], NBHDL customers represent approximately 88% of the total customer base and will be responsible for approximately 88% of these additional funds. These additional costs represent harm to NBHDL customers when compared to the status quo.

10. The Applicant has submitted that the incremental one-time transaction and transition costs of approximately $600k[12] are not actually a cost to customers and will not be recovered from them since they will be funded through residual [13] or retained [14] earnings. The Applicant subsequently corrected the “retained” earnings reference to indicate that the costs would be paid out of “current” earnings[15]. Employing this terminology to describe the funds used to pay for these expenses does not disguise the fact that all funds come from customers through the delivery rates paid by them. These funds, whether paid by customers in the past, currently or in the future, represent additional costs and are harmful to NBHDL customers compared to the status quo.

11. The OM&A costs noted in this application do not include depreciation and amortization costs or interest or PILS expenses. The increases in these costs which are also included in electricity delivery rates will have a harmful effect. A comparison of the 2018 financial statements of ERHDC [16] and of NBHDC [17] and the 2022 pro forma financial statement of the new NBHDL[18] interest costs will increase by approximately $465,000.

12. Loan principal payments are not deductible for tax purposes and are paid out of after tax cash. The tax on $8 million dollars at today’s rates will amount to an over $2.1 million ($8,000,000/79%)*21%). OM&A costs also do not take into account the $8 million in purchase price loan principal repayments which must be supplied by customers.

13. It will require at least 7 years from a rate rebasing standpoint and 25 years for NBHDL customers to repay the purchase price loan being undertaken by the new NBHDL. Based on this lengthy time period and the all too common inclination of

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[10] Purchase Price – Amortization Schedule.xlsx
[11] Application – Page 22 - Table 6-2
[12] Argument – Page 11 - 34
[13] IRR – Staff 1 - Page 5 - Lines 20 and 22 - Staff 2 - Page 6 - Line 33 and Argument - Page 8 - 30(k)
[14] IRR – Staff 2 – page 7 – Line 8 and DDR 12 - Page 53 – Line 11
[15] PO3 Response to Donald D. Rennick Submissions - Page 10 - 50
[16] IRR – SEC-3
[17] Ibid
[18] IRR – Staff 7 (b)

forecasts to fail to correctly identify problems that may arise from an operational and financial standpoint increases the risks involved.

14. The distance between the two operations of 175km and over 2 hours [19] in driving time has not been sufficiently addressed in the evidence supplied. The fact that the service areas are not contiguous is not conducive to efficient operations and is a negative feature of the amalgamation.

15. The OEB criterion for approval of this application is the “no harm” test. It appears doubtful that any member of the NBHDL board or the directors of any operation would have approved any financial action based on this test. The Applicant has been less than direct about the details concerning the agreement approval process[20]. The concern is that the NBHDL administration has obtained board approval suggesting that benefits will accrue to NBHDL customers when the application does not support this fact.

16. This amalgamation will benefit the Town of Espanola and Township of Sables-Spanish Rivers who will receive $8 million in cash. To suggest that this benefit will come with “no harm” and will be without cost to ratepayers is to deny reality. These costs will require additional funds and be paid for by the customers of ERHDC and NBHDL through delivery rates.

17. LDC’s are local municipal utilities that were mandated by the government of the day to incorporate. The beneficial owners and shareholders are exactly the same group of taxpayers who are supplying the funds to deliver the electricity delivery services. Government policy aside, the continuing charade that funds derived from any return on equity amounts included in electricity delivery rates is somehow beneficial to the same people who supplied the funds defies logic.

18. This is especially true since in addition to mandating incorporation, the government effectively changed the utilities tax-free status to one which requires the payment of amounts equal to that of a taxable corporation. According to the evidence [21], the tax liability in 2022 alone will be $788,770 which is an increase of $800,000 over the 2018 tax liability. These tax costs ha not been reflected in the total estimated savings forecasts.

19. The evidence contained in this application does not support the “no harm” test for the customers of NBHDL. The application contains no evidence that the amalgamation makes any rational sense from a business perspective. It is clear that from the evidence that the only real result of the amalgamation will be to obligate the customers of NBHDL

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[19] Application – Page 20 – Lines 10 and 12
[20] IRR - DDR-2 –Page 40 – Line 18
[21] IRR - Staff-7 and SEC-3

to, in effect, finance a reduction in the ERHDC per customer OM&A costs which as noted is a situation that is not of their making.

20. The statutory objectives considered for approval of this application are those set out in section 1 of the *Ontario Energy Board Act, 1988*. If the proposed transaction has a positive or neutral effect on the attainment of these objectives, the OEB will approve the application. It is submitted that the transaction does not meet those objectives on price and should be denied.

All of which is respectfully submitted.

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