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 a Motion to Review and Vary the Ontario Energy Board's Decision and Order dated April 23, 2019 re. Niagara-on-the-Lake Hydro Inc.'s 2019 Distribution Rate Application (EB-2018-0056).

AND IN THE MATTER OF Rules 8 and 40, 42 and 43 of the *Rules of Practice and Procedure* of the Ontario Energy Board.

REPLY SUBMISSIONS OF NIAGARA-ON-THE-LAKE HYDRO INC.

1. NOTL Hydro's motion seeks review and variance of those portions of the Decision in its cost of service rate proceeding (EB-2018-0056) in which the OEB determined NOTL Hydro's Operating, Maintenance and Administration (OM&A) budget for 2019. NOTL Hydro's Notice of Motion requests an Order approving a revised 2019 OM&A budget of $2,964,765 for NOTL Hydro.

2. NOTL Hydro's submissions in support of the motion were set out in the Notice of Motion, and in Supplementary Submissions filed on June 20, 2019.

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

4. These Reply Submissions set out NOTL Hydro's response to the arguments advanced by the other parties in this motion. In addition to the items set out herein, NOTL Hydro repeats and relies on the positions taken and arguments set out in its earlier submissions.

Threshold Test and Ability of the Review Panel to Review and Vary the Decision

5. NOTL Hydro has explained why it meets the Board's "threshold test" for review motions as set out in the NGEIR Review Motion decision and subsequent cases.[4] Each of the four

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[1] OEB Staff Submission, July 11, 2019 (OEB Staff Submission).
[2] Submissions of the School Energy Coalition, July 11, 2019 (SEC Submissions).
[3] Submission of the Vulnerable Energy Consumers Coalition, July 11, 2019 (VECC Submission).
[4] Notice of Motion, paras. 13-17 and 43-44; and Supplementary Submissions, paras. 6-9.

errors set out in the Notice of Motion raises material questions about the correctness of the Decision. The Decision fails to consider and is contrary to the evidence before the presiding member about the OM&A budget. Correcting the four identifiable errors will materially impact the Decision.

6. This is not a situation where the applicant is seeking to simply re-argue the case that it has already submitted.[5] NOTL Hydro's motion explains that the Board's Decision on the 2019 OM&A budget failed to consider or address the relevant evidence in support of that budget, relying instead on high-level adjustments to the last Board-approved budget (from 2013). It is not a re-argument to highlight the errors where the Board failed to consider and take account of the evidence about the constituent elements of a test year OM&A budget within a cost of service proceeding.

7. Similarly, it is not a re-argument of the original case to point to the errors where the Board failed to include and give NOTL Hydro the benefit of relevant and material inputs and adjustment factors when the Board applied its own formulaic or "yardstick" approach to setting NOTL Hydro's test year OM&A budget. NOTL Hydro's motion sets out these items and explains how the Board's failure to address and account for each item led to material errors in the Decision.

8. The Review Panel considering this motion is in the same position as the presiding member who considered the issues initially. There was no oral hearing, and the record for this motion is the same as what was before the presiding member who issued the Decision.[6] The issues raised in this motion are discrete and not dependent on any other aspects of the Decision outside of the OM&A budget, and all the relevant evidence has been provided in NOTL Hydro's Motion Record.

9. As set out in Part IV of the *Rules of Practice and Procedure*, the Board may vary a decision where there is an error.

10. In this case, the Review Panel is well-positioned to determine that there were errors in the Decision. As described below, the OEB's ratemaking framework contemplates that a distributor's rates are reset each five years based on actual costs (cost of service), and

[5] In response to SEC Submissions, para. 2; and VECC Submission, para. 5.
[6] Contrary to the VECC Submission, para. 22.

requires detailed evidence detailing such costs. It is only in the years between rebasing cases that rates are set on a formulaic basis. Where the Board disregards all the detailed (and required) evidence and instead uses a formulaic approach to reset rates in a cost of service case, then a cost of service determination never happens. NOTL Hydro submits that a cost of service decision that fails to take account of the actual costs included in the forecast budget is neither correct nor reasonable. There are further errors where (as is the case in the Decision) the formulaic approach used by the Board in place of a cost of service approach fails to include relevant inputs and adjustment factors, thereby decreasing the resulting approved budget below what it should be. The errors in the Decision have resulted in an OM&A budget that is materially lower than would have been approved absent the errors.

Errors in the Decision

11. NOTL Hydro's Notice of Motion describes and details the four errors in the Decision. The other parties take issue with each of these items. Below is NOTL Hydro's response to those submissions.

(i) Failure to consider NOTL Hydro's evidence about forecast and actual costs

12. As explained in the Notice of Motion, the "Findings" part of the Decision on NOTL Hydro's OM&A budget made no reference at all to any of the relevant and required evidence about the components of NOTL Hydro's actual forecast OM&A costs.[7] Instead, a "yardstick" approach was used to set a budget by way of adjustments to the prior Board-approved budget.[8] No reference was made to the fact that NOTL Hydro's customers are pleased with the reliable and responsive service that they are receiving, and have not expressed concerns with the costs of that service.[9]

13. Both SEC and OEB staff have argued that there is sufficient historical precedent for using a formulaic approach to determining appropriate OM&A, and there is no need to look at the

[7] Notice of Motion, paras. 23-23.
[8] Decision, pages 10-11.
[9] Exhibit 1 – Administrative Documents – Appendix 1H – CGC Customer Engagement Report NOTL Hydro, May 2018.

utility's actual costs.[10] SEC goes so far as to suggest that the Board's role as a market proxy does not require it to look at actual costs, but instead to look only at prices charged.[11]

14. While NOTL Hydro acknowledges that the Board may use a variety of methods to set just and reasonable rates, the fact that NOTL Hydro's 2019 rates are being set on a "cost of service" basis leads to the conclusion that consideration of actual forecast costs should be the first part of any review.[12] Otherwise, there is a never-ending disconnect between the utility's costs and its rates. The importance of reviewing actual costs is amplified by the particular circumstances of the applicant utility – where, as is the case with NOTL Hydro, the utility has extraordinary assets (transmission) and is experiencing high-growth and increasing customer demands, then a review of actual costs is essential.

15. SEC indicates that NOTL Hydro has failed to provide a single citation to support the statement that failure to look at forecast costs in a cost of service proceeding is contrary to policy and previous decisions of the Board.[13] NOTL Hydro's Notice of Motion made reference to the OEB's Renewed Regulatory Framework (RRFE) and Filing Guidelines in support of its position.[14] More detail is set out below.

16. The OEB's RRFE explains that under its 4th Generation IR method, "going in" rates are determined in a single forward test-year costs of service review, and subsequently indexed (adjusted) under the 4th generation price cap index formula.[15] The OEB's Handbook for Utility Rate Applications describes what is meant by "cost of service", indicating that:

> Cost of service is the total cost for a utility to provide service to its customers. A cost of service application is a detailed presentation of a utility's costs. The OEB reviews a cost of service application and decides the rates that a utility will charge its customers. The OEB examines the utility's operating, maintenance

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[10] OEB Staff Submission, pages 10-11; and SEC Submissions, paras, 19-22.
[11] SEC Submissions, para. 23.
[12] Indeed the Decision itself seems to acknowledge this, in the first part of the "Findings" on the OM&A budget issue, where it states that "The approval of the OM&A budget is a significant component of the regulatory exercise which is intended to achieve both the recognition of prudent proposed expenditures and encourage continuous improvement in utility performance." (page 10).
[13] SEC Submissions, para. 21.
[14] Notice of Motion, paras. 21 and 22.
[15] Report of the Board: A Renewed Regulatory Framework for Electricity Distributors: a Performance Based Approach, October 18, 2012, pages 7 and 13.

and administrative expenses and capital expenditures, as well as the expected number of customers and total amount of energy delivered.[16]

17. The OEB has prescribed the filing requirements for cost of service rate applications by electricity distributors. As set out in the OEB's guide, "the filing requirements have been established to require complete and transparent information sufficient to inform the Board and interested parties of all material facts related to the distribution of electricity by an electricity distributor in order to set rates".[17]

18. Taking these items together, it is clear that in a cost of service application the OEB requires detailed evidence about a utility's costs and uses that information to determine what rates should be charged.

19. VECC's allegation that an I-X approach to ratemaking should be maintained even at rebasing (so that efficiency gains made during IRM are not lost)[18] ignores the OEB's direction to approach ratemaking differently in a rebasing year. NOTL Hydro might have preferred to remain indefinitely on 4th Generation IRM ratemaking, since it continued to earn its rate of return. However, Ontario distributors are expected to rebase and go through a cost of service proceeding each five years. NOTL Hydro believes it is a reasonable expectation that its actual costs will be examined in that process. Additionally, the assertion that efficiencies gained during IRM are lost through a cost of service rebasing is not true in NOTL Hydro's case. Had NOTL Hydro remained on IRM, then its 2019 rates and revenues (inclusive of ICM) would have been higher than the rates that will result from this cost of service proceeding, even with the corrections to the Decision requested in this motion. Cost of service proceedings (which require the applicant to detail its updated costs, inclusive of gained efficiencies) pass along the efficiencies from the IRM term to ratepayers, since these are embedded in the utility's current costs.

20. Parties point to cases where the OEB has adopted an "envelope" approach to set a distributor's OM&A budget in a cost of service proceeding, and indicate that this shows that the Board need not undertake an evaluation of actual forecast costs when approving a

[16] Handbook for Utility Rate Applications October 13, 2016, page 37 (in Glossary of Terms).
[17] Filing Requirements For Electricity Distribution Rate Applications - 2018 Edition for 2019 Rate Applications – Chapter 2, Cost of Service, July 12, 2018.
[18] VECC Submission, para. 16.

budget.[19] NOTL Hydro does not agree. The excerpt from a Hydro One decision cited by SEC indicates that the OEB may choose to approve an "envelope" OM&A budget which the utility can spend as it sees fit, rather than having to confine future spending to specific items.[20] That does not mean, though, that the decision about the size/amount of the OM&A envelope should be made without considering the distributor's actual costs. Different distributors will have different cost requirements. The budget-setting approach used by the Board must fit the particular conditions and requirements of the applicant. That is particularly the case for a distributor like NOTL Hydro which is different from many other LDCs, because while its existing rates are low, it is experiencing high growth in customers, load and demand, and has significant large transmission asset investments. These are items not captured by a one-size-fits-all formulaic approach to set an OM&A budget envelope.

21. Recent OEB decisions considering an envelope approach to OM&A budget approval have typically looked at both formulaic adjustments and actual costs.[21] Indeed, even in the Hydro One case cited by SEC, the Board's determination of an OM&A budget started from an examination of the "totality of the evidence developed throughout the case", including in that case the specific evidence about compensation and vegetation management costs.[22]

22. SEC suggests that it was NOTL Hydro that introduced the formulaic approach adopted by the OEB in the Decision to evaluate the OM&A budget, and therefore NOTL Hydro cannot now complain that such an approach was used in place of considering the evidence of actual costs.[23] That submission misses the fact that the formulaic approach included in NOTL Hydro's "Additional Evidence" was indicated to be supplementary evidence meant to provide further context and explanation for the actual forecast costs.[24]

23. NOTL Hydro believes it is worth distinguishing between its as-filed cost forecasts and the analyses designed to support those forecasts. NOTL Hydro's detailed line-by-line OM&A

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[19] OEB Staff Submission, pages 10-11; and SEC Submissions, paras. 19-22.
[20] SEC Submissions, para. 19, citing the EB-2009-0096 Hydro One Distribution Decision and Order (April 9, 2010) at page 12.
[21] See, for example, EB-2016-0105 (Thunder Bay Hydro), pages 4-6; EB-2015-0089 (Milton Hydro), pages 32 and 35-36; EB-2015-0072 Decision and Order (Grimsby Power), pages 4-6; and EB-2014-0073 Decision and Order (Festival Hydro), pages 8-9.
[22] EB-2009-0096 Hydro One Distribution Decision and Order (April 9, 2010), page 12.
[23] SEC Submissions, paras. 17-18.
[24] Exhibit 4 – OM&A Additional Evidence – page 8 of 15.

submission is included in Exhibit 4 of the prefiled evidence (including in Table 4.1) and in the Excel Chapter 2 Appendices of the prefiled evidence. NOTL Hydro then provided ten supporting analyses designed to demonstrate the appropriateness of the submission.[25]

24. None of these supporting analyses was used by NOTL Hydro to determine its as-filed OM&A budget forecast for 2019. The determination of the OM&A budget was done using a line-by-line review by NOTL Hydro management. The supporting analyses were used to support the reasonableness of the submitted OM&A. This is made clear in NOTL Hydro's Argument in Chief, which indicated that the components of the OM&A budget include the required expenditures to maintain safe, reliable and customer-focused operations and then described four other analyses that confirm the reasonableness of the budget.[26]

25. Rather than reviewing the actual forecast cost information filed by NOTL Hydro, the Decision referred to and inappropriately modified one of the additional analyses from the Additional Evidence and used that approach as the *sole* basis to set a 2019 OM&A budget. This approach largely replicates the annual IRM model used in the intervening years. As NOTL Hydro pointed out in its Notice of Motion[27], if the intent of the Cost of Service application is to "re-set" rates based on real costs then the same type of formulaic methodology used for IR years should not be used in the rebasing year.

(ii) Failure to include the impact of growth in NOTL Hydro's kWh delivered and system peak capacity

26. The second error identified by NOTL Hydro was that the Decision failed to include all relevant factors from the PEG model when applying a formulaic approach to set an OM&A budget amount. Specifically, NOTL Hydro asserts that the Decision erred by not including the impact of the growth in NOTL Hydro's kWh delivered and system peak capacity over the

[25] These supporting analyses included (i) a breakdown of the 2014-2019 growth in OM&A by causal factors (pages 5-7 of Exhibit 4 of the prefiled evidence); (ii) a year-to-year analysis by OM&A cost drivers (pages 9-14 of Exhibit 4 of the prefiled evidence); (iii) a year-to-year OM&A variance analysis (pages 14-17 of Exhibit 4 of the prefiled evidence); (iv) an OM&A per customer analysis (pages 18-20 of Exhibit 4 of the prefiled evidence); (v) a breakdown of OM&A costs by program delivery (pages 21-41 of Exhibit 4 of the prefiled evidence); (vi) a review of historical rate performance (page 2 of the Additional Evidence on OM&A); (vii) a comparison with expected rates based on customer density (pages 3-4 of the Additional Evidence on OM&A); (viii) a review of annual rate changes compared to inflation (pages 4-5 of the Additional Evidence on OM&A); (ix) a review of PEG performance (pages 6-7 of the Additional Evidence on OM&A); and (x) an alternative cost driver analysis (pages 8-13 of the Additional Evidence on OM&A).
[26] Argument in Chief, para. 42, Motion Record, Tab 5(1).
[27] Notice of Motion, para. 22.

years from 2014 to 2019 when determining a reasonable level of OM&A costs for the Test Year.[28]

27. OEB Staff argued that the use of the PEG report was as a "yardstick" against which to measure NOTL Hydro's request and that it was not used as a "determinative" manner.[29] NOTL Hydro disagrees. The Decision calculates NOTL Hydro's allowable OM&A using parts of the PEG model. This is a "determinative" use of the PEG report.

28. OEB Staff, SEC and VECC all argued against NOTL Hydro's position on the motion, stating that the Board had reviewed NOTL Hydro's position on the use of the PEG factors for load growth (kWh load) and system peak capacity and decided they should not be applied.[30] OEB Staff noted that the Decision states:

> NOTL Hydro also suggested additional load and peak growth factors as escalators to the OEB-approved OM&A. However, there is no indication that any increases caused by these factors would not be captured in whole or in part by the customer growth factor.[31]

29. It is this part of the Decision that is the error. The Pacific Economics Group, in doing the analysis to create the PEG model, very clearly determined that both system peak and kwh load were statistically significant. This means that they are not captured by customer growth but are in addition to it.[32] The Board erred by ignoring this fact when determining the items that would be seen to increase NOTL Hydro's costs using the PEG model.

30. SEC noted that the PEG model is based on total costs and not just OM&A, and argued that the growth in NOTL Hydro's kWh delivered and system peak capacity does not impact OM&A expenses.[33] NOTL Hydro agrees that the PEG model is based on total costs. Importantly, however, the model does not measure the impact of any of the three factors on OM&A and/or capital expenses in isolation. NOTL Hydro's evidence is that applying a customer growth factor on its own does not capture all of the operating costs pressures

[28] Notice of Motion, paras. 25-32.
[29] OEB Staff Submissions, page 7.
[30] OEB Staff Submission, pages 6, 7 and 12; SEC Submissions, paras. 26-34; and VECC Submission, paras. 8-9.
[31] Decision, page 11.
[32] Pacific Economics Group Research, LLC, Productivity and Benchmarking Research In Support Of Incentive Rate Setting in Ontario: Final Report to the Ontario Energy Board, November 2013, at page 10.
[33] SEC Submissions, para. 28.

faced by a utility whose load and customer base are both growing.[34] This is confirmed in the graph in NOTL Hydro's Notice of Motion that illustrates the impact of using all of PEG's statistically significant variables versus the approach adopted in the Decision.[35]

31. NOTL Hydro presented an approach using the PEG model as a way to confirm the reasonableness of the OM&A budget. NOTL Hydro never requested that its allowable OM&A be determined using the PEG model. That was a decision of the Board. However, if the Board is to take this approach of using the PEG model, then it should be done in a manner consistent with the statistical determination of the model.

(iii) Failure to include relevant new and increased costs

32. The third error identified by NOTL Hydro was the lack of explanation given to the new and increased costs (extraordinary costs) that were denied in the Decision. As detailed in the Notice of Motion, the Decision provides no explanation as to why some of these costs were accepted and others were not.[36]

33. Much is made in the intervenor arguments about the expectation that LDCs will find efficiencies to cover new costs.[37] The expectation that LDCs should find efficiencies to cover new or growing costs arises many times during the rate making process. This includes when new programs are introduced (OESP, LEAP, OREC, etc.), within the annual IRM process (which includes efficiency by way of stretch factors), when customer demands change (payment systems, access to data, web-based tools) and in the cost of service process itself. There is only so much efficiency that can be realized; especially if the LDC is already efficient. NOTL Hydro has commented many times on its already low rates. It is also earning close to its regulated rate of return. This can only be accomplished if costs are being appropriately managed. It is not clear that ever-increasing customer and operational requirements (like those whose costs were dismissed without explanation in this case) can be accommodated by finding yet to be identified efficiencies while maintaining current service levels.

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[34] Response to SEC Supplementary Interrogatory #41.
[35] Notice of Motion, para. 31.
[36] Notice of Motion, paras. 33-35.
[37] SEC Submissions, para. 37; and VECC Submission, para. 21.

34. OEB Staff and SEC argued that there is no error in a finding that extraordinary costs can be accommodated in an OM&A budget envelope.[38]

35. NOTL Hydro notes that the disallowed costs of $138,605 represent 5% of the requested OM&A expenditure; a significant amount. They also represent 58% of the new or increased costs included in this analysis. The only discussion in the Decision is the line "This envelope must then be adjusted to recognize expenditures that are not simply improvements, updates, or changes to operations driven by management operational decisions or directions."[39] The Decision contains no explanation or details as to why any of the disallowed costs (as detailed in the chart in the Notice of Motion) meet these criteria. That is the error.

(iv) Failure to include previously capitalized costs in base OM&A costs

36. The fourth error identified by NOTL Hydro was that the Decision failed to include previously capitalized labour costs in the base 2014 OM&A budget that was adjusted to arrive at the 2019 Test Year budget.[40] If the Board chooses to adopt an adjustment formula to convert 2014 costs to 2019 costs, then all relevant items that are part of the utility's costs at the outset should be part of the adjusted base.

37. NOTL Hydro acknowledges the argument from SEC[41] that the amount in issue here ($25,269) would not be material on its own. However, given the materiality of the other errors included in this motion it is reasonable to include this item along with the others.

Conclusion

38. For the reasons set out in the Notice of Motion, Supplementary Written Submissions and Reply Submissions, NOTL Hydro respectfully requests that the Decision be adjusted to approve a 2019 Test Year OM&A budget of $2,964,765. This will allow NOTL Hydro to continue to provide reliable, customer-focused and cost-effective service that its customers expect and value.

39. In the event that there is a finding that the Decision contains errors, but the Review Panel is

[38] OEB Staff Submission, pages 7 and 12; and SEC Submissions, paras. 35-37.
[39] Decision, page 11.
[40] Notice of Motion, paras. 36-38.
[41] SEC Submissions, para. 39.

not prepared to adjust the OM&A budget as requested, then NOTL Hydro requests that the Board make orders for the errors in the Decision to be corrected through an appropriate process.

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