Ontario Energy Board | Commission de l'énergie de l'Ontario

BY EMAIL

September 23, 2019

Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto ON M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Kitchener-Wilmot Hydro Inc. (Kitchener-Wilmot Hydro)
Application for 2020 electricity distribution rates
OEB Staff Submission
Ontario Energy Board File Number: EB-2019-0049

In accordance with Procedural Order No. 4, please find attached OEB staff's submission in the above proceeding.

Yours truly,

Original Signed By

Donald Lau
Project Advisor – Rates Major Applications

Encl.

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ONTARIO ENERGY BOARD

STAFF SUBMISSION ON SETTLEMENT PROPOSAL

2020 ELECTRICITY DISTRIBUTION RATES

Kitchener-Wilmot Hydro Inc.

EB-2019-0049

September 23, 2019

INTRODUCTION

Kitchener-Wilmot Hydro Inc. (Kitchener-Wilmot Hydro) filed a cost of service application with the Ontario Energy Board (OEB) on April 30, 2019 under section 78 of the *Ontario Energy Board Act*, *1998* seeking approval for changes to the rates that Kitchener-Wilmot Hydro charges for electricity distribution, to be effective January 1, 2020. The parties to the settlement proposal are Kitchener-Wilmot Hydro and the following approved intervenors in the proceeding: Energy Probe, School Energy Coalition, and Vulnerable Energy Consumers Coalition, collectively called the Parties.

The OEB issued an approved issues list for this proceeding on August 13, 2019. A settlement conference was held on August 14, 2019 and August 15, 2019 and Kitchener-Wilmot Hydro filed a settlement proposal setting out an agreement among all the Parties to the proceeding on September 13, 2019.

The settlement proposal represents a full settlement of all issues in Kitchener-Wilmot Hydro's application.

For a typical residential customer with a monthly consumption of 750 kWh, the total bill impact under the filed settlement proposal is an increase of $5.52 per month before taxes or 5.97%.

This submission is based on the status of the record as of the filing of Kitchener-Wilmot Hydro's settlement proposal and reflects observations which arise from OEB staff's review of the evidence and the settlement proposal. It is intended to assist the OEB in deciding upon Kitchener-Wilmot Hydro's application and the settlement proposal.

Settlement Proposal

OEB staff has reviewed the settlement proposal in the context of the objectives of the *Renewed Regulatory Framework*[1], the *Handbook for Utility Rate Applications*[2], applicable OEB policies, relevant OEB decisions, and the OEB's statutory obligations. OEB staff submits that the settlement proposal reflects a reasonable evaluation of the distributor's planned outcomes in this proceeding, appropriate consideration of the

[1] Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach, October 18, 2012
[2] Handbook for utility Rate Applications, October 13, 2016

relevant issues, and ensures that there are sufficient resources to allow Kitchener-Wilmot Hydro to achieve its identified outcomes in the five years that will follow.

OEB staff further submits that the explanations and rationale provided by the Parties are adequate to support the settlement proposal and that the outcomes arising from the OEB's approval of the settlement proposal would adequately reflect the public interest and would result in just and reasonable rates for customers.

Below, OEB staff provides specific submissions on the following issues, which are a subset of the issues listed in the settlement proposal:

- Issue 1.1 Capital
- Issue 1.2 Operating, Maintenance, and Administration (OM&A)
- Issue 2.0 Revenue Requirement
- Issue 3.0 Load Forecast, Cost Allocation, and Rate Design
- Issue 4.0 Accounting
- Issue 5.1 Are the Specific Service Charges appropriate?
- Issue 5.2 Is the proposed effective date January 1, 2020 appropriate?

Issue 1.1 Capital

In its original application evidence, Kitchener-Wilmot Hydro proposed a total net capital expenditure of $20.6 million for the 2020 test year. This represented an increase of 20% from the 2014 approved total net capital expenditures or an average yearly increase of 3.3%. After interrogatories, Kitchener-Wilmot Hydro updated its total net capital expenditure to $22.2 million, mostly as a result of an updated cost estimate for the Customer Information System (CIS).[3] Kitchener-Wilmot Hydro stated that its service area is expected to see moderate urban growth and the downtown core is expected to see increased residential and commercial density. A key development project in the service area has been the Light Rail Transit (LRT), which has required Kitchener-Wilmot Hydro to complete line relocations. Kitchener-Wilmot Hydro continues to expect investments related to servicing new customers and relocation of distribution assets as a result of road authorities. There are also investments to renew the distribution system, which are driven by the condition of distribution assets. Noteworthy assets that Kitchener-Wilmot Hydro is intending to replace are power transformers, poles, and the conversion of assets from 8.32kV to 27.6kV. Kitchener-Wilmot Hydro is also planning to replace an existing 30 year old CIS through the 2019 and 2020 period.

[3] EB-2019-0049 Interrogatory Response, July 31, 2019 (2-Staff-8)

For the purposes of the settlement of all of the issues in this proceeding, the Parties have accepted that the level of planned capital expenditures and the rationale for planning and pacing choices are appropriate and adequately explained.

The largest category of capital expenditures in the test year is system renewal, which is approximately 40% of the total capital expenditures. It is almost double the actual system renewal spending in 2014. In addition, in 2014-2017 the LRT project had higher than expected costs[4], which resulted in the deferral of other planned capital expenditures such as system renewal expenditures that were originally planned in Kitchener-Wilmot Hydro’s 2014 cost of service application. OEB staff notes that while in the test year the system renewal spending is higher than historical, it is offset by lower system access spending. Taking into consideration the system renewal deferrals due to the increased cost of the LRT, OEB staff submits that Kitchener-Wilmot Hydro’s forecast system renewal spending in the test year is reasonable.

The asset condition assessment (ACA) showed that there were three station transformers that were in poor condition[5] and 20% of Kitchener-Wilmot Hydro’s wood poles were either in poor or very poor condition.[6] The reliability data also showed that defective equipment related outages are approximately one-third of the total outages experienced.[7] OEB staff submits that the ACA and reliability data support Kitchener-Wilmot Hydro’s capital investments.

Kitchener-Wilmot Hydro also provided its voltage conversion plans for the Township of Wilmot, which will eventually see the elimination of the 8.32kV distribution system.[8] This will eliminate the need for the seven distribution stations in the Township of Wilmot and reduce future costs to maintain/rebuild these stations, reduce line losses, improve the ability to connect distributed generation, and improve voltage regulation. OEB staff submits that Kitchener-Wilmot Hydro has put forth a reasonable plan to improve the distribution system and reduce long-term costs.

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[4] The drivers of the variances were a change in design scope to align with the final LRT design and additional system modifications after the initial plant relocation was completed (EB-2019-0049 OEB Staff Pre-settlement Clarification Questions, August 14, 2019, 2-Staff-80).
[5] EB-2019-0049 Exhibit 2 - Appendix L: 2018 Asset Condition Assessment Report, p.36
[6] EB-2019-0049 Exhibit 2 - Appendix L: 2018 Asset Condition Assessment Report, p. 54
[7] EB-2019-0049 Exhibit 2 – Distribution System Plan, pp. 50-51
[8] EB-2019-0049 Interrogatory Responses, July 31, 2019 (2-Staff-15)

Kitchener-Wilmot Hydro is also replacing a CIS that is over 30 years old and which uses a programming language that is now obsolete. Kitchener-Wilmot Hydro was originally part of a consortium with three other local distribution companies (LDCs) that tried to find an affordable CIS solution but was ultimately disbanded due to higher than expected solution costs. Kitchener-Wilmot Hydro then looked at options such as restarting the consortium or sharing another LDC's CIS platform but these options were rejected due to the risk of the existing CIS failing before the solution could be put in place and costs. Kitchener-Wilmot Hydro eventually used the CIS solution from the consortium and asked vendors to submit bids. OEB staff submits that this investment is reasonable. The CIS is past its end-of-life and Kitchener-Wilmot Hydro has shown consideration to multiple alternatives to the replacement of the CIS, evaluation of multiple bids for the alternative, and a phased project approach to control bill impacts.

As a result, in the context of the settlement proposal, OEB staff has no concerns with the 2020 capital budget included in the settlement proposal.

Issue 1.2 Operating, Maintenance, and Administration (OM&A)

In its original application evidence, Kitchener-Wilmot Hydro proposed total OM&A spending of $22.0 million for the 2020 test year. This represented an increase of 19.6% from the 2014 approved OM&A or an average yearly increase of 3.3%. Kitchener-Wilmot Hydro attributed this increase to a number of factors including: (i) operating costs for the new CIS (previous system was maintained by in house programmers), (ii) increases in OEB Assessment Fees, (iii) costs associated with preparation of the Cost of Service application, (iv) change to monthly billing, (v) third-party billing costs, (vi) reliability improvements, (vii) storms and major events, and (viii) cyber security. After interrogatories, Kitchener-Wilmot Hydro updated its OM&A to $22.165 million as a result of shuffled positions after discontinuing Conservation Demand Management (CDM) activities[9] and update to operating costs for the new CIS.[10]

The Parties agreed to a reduction of approximately $1 million to Kitchener-Wilmot Hydro's proposed OM&A spending to $21.165 million. This revised amount is an increase of 15.3% from the 2014 approved OM&A or an average yearly increase of 2.6%. OEB staff notes that Kitchener-Wilmot Hydro is in the Group 2 cohort as per the *Empirical Research in Support of Incentive Rate-Setting: 2018 Benchmarking Update*[11]

[9] EB-2019-0049 Interrogatory Response, July 31, 2019 (1-SEC-3)
[10] EB-2019- Interrogatory Response, July 31, 2019 (2-VECC-5)
[11] Report to the Ontario Energy Board – "Empirical Research in Support of Incentive Rate-Setting: 2018 Benchmarking Update", prepared by Pacific Economics Group LLC., August 2019

and has been in this group since 2014. The settlement proposal also showed, by using the Pacific Economics Group forecasting model, an estimated efficiency assessment of 19.23% below predicted costs. OEB staff further notes that although Kitchener-Wilmot Hydro is forecasting below predicted costs, the settled OM&A envelope still represents an approximate 8.7% increase from the 2018 actual OM&A and should ensure Kitchener-Wilmot Hydro has the resources to maintain a safe and reliable distribution system. In the context of the settlement proposal, OEB staff does not have concerns with the proposed 2020 test year OM&A of $21.165 million.

Issue 2.0 Revenue Requirement

The Parties have agreed to a service revenue requirement of $46.8 million and a base revenue requirement of $43.6 million. This reflects a reduction of approximately $1 million in OM&A and updated Payment In Lieu of Taxes (PILs), which resulted in zero PILs, as per Kitchener-Wilmot Hydro's interrogatory updates.[12]

The federal *2019 Budget Implementation Act* (Bill C-97) was given royal assent on June 21, 2019. Among other things, Bill C-97 made changes to the federal *Income Tax Act*, including new accelerated capital cost allowance (CCA) deductions on capital assets acquired after November 20, 2018. Through interrogatories, OEB staff asked Kitchener-Wilmot Hydro to calculate the impacts of the new accelerated CCA rules.[13] OEB staff further asked if a smoothing technique would be appropriate to account for volatility in PILs resulting from Bill C-97.[14] In Kitchener-Wilmot Hydro's interrogatory response, it supported a smoothing mechanism and noted that the "smoothing technique would leave both the customer and the LDC unharmed by this recent legislation".[15]

The Parties agreed to remove the CCA smoothing methodology used in the calculation of PILs, as there was no impact under either approach. OEB staff notes that, in this case, the end result under either calculation method results in PILs of nil. OEB staff submits that PILs has been appropriately calculated.

Kitchener-Wilmot Hydro also stated that it would update the cost of capital parameters when the 2020 parameters are issued. OEB staff submits that this is appropriate and that Kitchener-Wilmot Hydro should file a draft rate order once the 2020 cost of capital parameters are issued.

[12] EB-2019-0049 Interrogatory Response, July 31, 2019 (4-Staff-46)
[13] Ibid.
[14] Ibid.
[15] Ibid.

Issue 3.0 Load Forecast, Cost Allocation, and Rate Design

Load Forecast

In the context of the settlement proposal, OEB staff does not have any concerns with the proposed load forecast of 1,748 GWh, 2,176,452 kW, and 101,587 customers and connections as shown in tables 3.1A and 3.1B of the settlement proposal. OEB staff submits that the agreed upon load and customer connection forecasts are appropriate.

For the purposes of the settlement of all of the issues in this proceeding the Parties agreed that the total CDM adjustment of 24.3 GWh proposed by Kitchener-Wilmot is appropriate. As shown in Table 3.1C of the settlement proposal, the allocation of CDM to rate classes was revised such that 14% is attributed to GS < 50 kW and 86% attributed to GS > 50 kW (residential was changed from 1% to 0% and GS<50 kW was changed from 13% to 14%). OEB staff notes that this reasonably reflects the Minister's directive to the Independent Energy System Operator on March 20, 2019. The proposed Lost Revenue Adjustment Mechanism Variance Account (LRAMVA) target is provided in Table 3.1D. OEB staff submits that the agreed upon CDM adjustment and LRAMVA target are appropriate.

Cost Allocation

As part of the settlement proposal, the Parties agreed that the billing and collecting weighting factors used for cost allocation would be updated. The agreed upon update, as set out in Table 3.2B, is to exclude costs associated with account setup and disconnections.

With respect to revenue to cost ratios, the Parties agreed on the ratios set out in Table 3.2A. This reflects a reduction in the street lighting revenue-to-cost ratio from 127.58% to 120%. Offsetting adjustments were made to the GS > 50 kW and Embedded Distributor rate classes, both of which moved to 97.30% from 97.17% and 93.31% respectively.

In the context of the settlement proposal, OEB staff does not have any concerns with the cost allocation.

Rate Design

OEB staff notes that the transition to fully fixed residential rates was concluded in 2019. As a result, there are no impacts arising from the residential rate design policy.

In the proposed settlement proposal, the Parties agreed that the fixed charge for the GS > 50 rate class should not be more than the current fixed rate. All other rate classes are proposed to maintain the existing fixed-variable split. In the case of three rate classes, this results in an increase to the fixed charge where the current fixed charge is already above the ceiling value established by the minimum system with peak load carrying capacity adjustment. These three rate classes and adjustments are detailed as follows:

	Existing Fixed Charge	Ceiling[16]	Proposed Fixed Charge
GS < 50 kW	$27.76	$18.05	$28.61
Large Use	$17,188.81	$88.74	$17,727.10
Unmetered Scattered Load	$7.43	$7.20	$7.66

OEB staff notes that it is not unusual for existing fixed charges to be significantly above the ceiling. However, section 2.8.1 of the Filling Requirements for Electricity Distribution Rate Applications states:

> If a distributor's current fixed charge for any non-residential class is higher than the calculated ceiling, there is no requirement to lower the fixed charge to the ceiling, nor are distributors expected to raise the fixed charge further above the ceiling for any non-residential class.[17]

OEB staff further notes that in several past rate cases, the OEB has permitted electricity distributors to increase fixed charges that were already above the ceiling. These include InnPower[18] and Horizon.[19]

OEB staff notes that generally speaking, the fixed charge is not expected to increase if it is already above the ceiling per the OEB's policy on this matter. However, in the context of the complete settlement proposal, and in the context of previous proceedings noted above, OEB staff accepts the rate design.

[16] The ceiling is established by the minimum system with peak load carrying capacity adjustment, and is calculated by the Cost Allocation Model, sheet O2 Fixed Charge|Floor|Ceiling.
[17] Ontario Energy Board Filing Requirements For Electricity Distribution Rate Applications – 2018 Edition for 2019 Rate Applications- Chapter 2, section 2.2.2.3.
[18] EB-2016-0085.
[19] EB-2014-0002.

Issue 4.0 Accounting

Kitchener-Wilmot Hydro proposed to dispose of its Group 1 (credit of $589,646) and Group 2 (debit of $853,884) Deferral and Variance Accounts (DVA) balances as at December 31, 2018 including forecasted interest through December 31, 2019. The Parties agreed with Kitchener-Wilmot Hydro's proposal for disposal of its Group 1 and Group 2 DVAs. The Parties further agreed to dispose of 2018 balances and forecasted balances for 2019 in the following Group 2 accounts: Account 1518 – Retail Cost Variance Account – Retail, Account 1548 – Retail Cost Variance Account – STR, Account 1508 – OEB Cost Assessment, and Account 1508 – Pole Rental Revenue. These accounts will be closed at December 31, 2019, and no further balances will be accumulated in these accounts.

OEB staff submits that it is appropriate to dispose of the 2018 Group 1 DVA balances on a final basis.

On July 20, 2018, the OEB issued a letter to all rate-regulated licensed electricity distributors, advising them that the OEB is undertaking an initiative to standardize the accounting processes used by distributors relating to Regulated Price Plan (RPP) wholesale settlements. This letter also stated that, effective immediately, the OEB will not be approving Group 1 rate riders on a final basis pending the development of this further guidance.

On February 21, 2019, the OEB issued its Accounting Procedures Handbook Update - Accounting Guidance Related to Commodity Pass-Through Accounts 1588 & 1589, outlining standardized requirements for regulatory accounting and RPP settlements that all distributors are expected to follow (Accounting Guidance). The Accounting Guidance is effective January 1, 2019, and was to be implemented by August 31, 2019.

In the OEB's *Addendum to Filing Requirements for Electricity Distribution Rate Applications – 2020 Rates* (the 2020 Filing Requirements Addendum), under Section 3.2.5.3, the OEB stated that, for 2020 rate applications, distributors are to provide a status update on the implementation of the new Accounting Guidance, a review of historical balances, results of the review, and any adjustments made to account balances. The 2020 Filing Requirements Addendum also states the following expectations for final disposition requests of commodity pass-through account balances:

- Any historical balances that were previously approved on an interim basis, or not approved at all, including the 2018 balances, have been reviewed in the context of the Accounting Guidance and are confident that there are no systemic issues with their RPP settlement and related accounting processes affecting those balances

- Any historical balances that were previously not approved by the OEB due to concerns noted have been assessed in the context of the updated Accounting Guidance. Any necessary revisions or adjustments made are documented, discussed in detail, quantified, and provided to the OEB for review prior to request for final disposition

OEB staff notes that in Kitchener-Wilmot Hydro's 2019 IRM rate decision[20], the 2017 commodity pass-through account balances were approved for disposition on an interim basis as the account balances were justified and were reasonable. In response to an interrogatory question[21], Kitchener-Wilmot Hydro confirmed that it had incorporated the OEB's Accounting Guidance into its settlement processes during 2019. Kitchener-Wilmot Hydro further stated "KWHI will not be revising any 2018 transactions as a result of implementing the new guidance. KWHI confirms that it has considered the Accounting Guidance and is of the view that no adjustments to balances are required, with the exception of a small true up balance that arose after the application was filed (9-Staff-67 and 9-Staff-68)."[22]

OEB staff submits that it is appropriate to dispose of the Group 2 DVA balances on a final basis.

OEB staff notes that Account 1518 – Retail Cost Variance Account – Retail, Account 1548 – Retail Cost Variance Account – STR, Account 1508 – OEB Cost Assessment, and Account 1508 – Pole Rental Revenue will no longer be applicable to Kitchener-Wilmot Hydro after its rates are rebased in this proceeding.[23] [24] [25] OEB staff submits that in the context of the settlement proposal, it is reasonable to dispose of the above accounts on a forecast basis in this proceeding, rather than deferring disposition of

[20] EB-2018-0048 Decision and Rate Order, December 13, 2018
[21] Responses to 9-Staff-65, July 31, 2019.
[22] Ibid.
[23] EB-2015-0304 Decision and Order – Energy Retail Service Charges p. 5
[24] OEB letter re: Revisions to the Ontario Energy Board Cost Assessment Model, February 9, 2016
[25] OEB letter re: Accounting Guidance on Wireline Pole Attachment Charges, July 20, 2018 p. 3

amounts pertaining to 2019 until Kitchener-Wilmot Hydro's subsequent cost-based rate application. OEB staff further submits that it is reasonable to close these accounts at December 31, 2019, as any variances between forecast and actual results in these accounts are expected to be insignificant, given that the nature of the transactions in these accounts can be forecast with reasonably high accuracy.

Issue 5.1 Are the Specific Service Charges appropriate?

Kitchener-Wilmot Hydro proposed to increase its Meter Removal without Authorization Charge from the current $60 to $355.

The Parties agreed that the proposed specific service charges were appropriate.

Kitchener-Wilmot Hydro provided a breakdown of the hours and labour required for the Meter Removal without Authorization Charge through interrogatories.[26] OEB staff submits that the Meter Removal without Authorization Charge is reasonable.

Issue 5.2 Is the proposed effective date January 1, 2020 appropriate?

In the settlement proposal, the Parties agreed that an effective date of January 1, 2020 is appropriate. OEB staff notes that the complete settlement proposal was filed on September 13, 2019. OEB staff submits that an effective date of January 1, 2020 is appropriate as the application was filed on time and there were minimal delays caused by the applicant.

All of which is respectfully submitted

[26] EB-2019-0049 Interrogatory Responses, July 31, 2019 (8-Staff-58)