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Our File No. EB-2020-0002

Ontario Energy Board
2300 Yonge Street
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Attn: Christine Long, Registrar and Board Secretary

Dear Ms. Long;

Re: EB-2020-0002 – Alectra 2021 Rates – SEC Final Argument

We are counsel for the School Energy Coalition. Pursuant to Procedural Order #1, these are SEC's submissions with respect to the above Application.

Our submissions are divided into five sections:

1. 2010 Global Adjustment error
2. Horizon ESM calculations and allocations generally
3. ICM Claims – Brampton
4. ICM Claim - Powerstream
5. Effective Date

2010 Global Adjustment Error

The single most substantial claim in the current Application is a request that the Board order recovery of $8.3 million[1] from customers as a result of an error made by Horizon, a predecessor of the Applicant, in 2010[2].

The initial disclosure of the error was curious. In Exhibit 3/1/8 the Applicant merely said that it had identified an error in 2010, had paid $8.1 million to IESO in 2019, and had included the amount in the December 31, 2019 HRZ Group 1 balance.

What the Application did not disclose, but came out in interrogatories, is two other salient facts:

a) The underpayment, $8.1 million, is made up of $4.0 million[3] of amounts related to the period 2011-2016, for which deferral and variance balances had been cleared on a final basis[4]. The remaining $4.1 million relates to 2017, which has been cleared on an interim basis, and 2018, which has not been cleared at all. An additional $0.2 million is being claimed as interest.

b) Almost all of the amount ($7.2 million out of $8.3 million[5]) is proposed to be collected from GS>50 customers in the HRZ over a one year period as part of the overall clearance of Group 1 accounts in 2021.

In addition to being the biggest amount in the Application, yet warranting only one page in the pre-filed evidence, the Applicant's proposal has a significant impact on certain customers, such as schools.

While SEC has been unable to find an express disclosure by the Applicant of that impact, it is possible to calculate it. For the schools in Hamilton and St. Catharines, for example, the Applicant seeks to impose a one-year, retroactive charge of more than $500,000[6]. To put that in context, the base distribution charges (fixed and variable) for HRZ schools are about $2.4 million per year, before this additional amount.

[1] VECC-8, p. 1.
[2] Ex. 3/1/8, p. 1.
[3] VECC-8, p. 1.
[4] SEC-20(b), p. 2.
[5] VECC-8, Tables 2-4.
[6] Calculated by taking $7.156 million allocated to GS>50 customers (which is the bulk of the schools), and dividing by the 5.125 million kW used for GS>50 Group 1 recoveries (G-Staff-2, Attach3, Sheet 7) to get a monthly cost per kW of $1.396. For a typical school, at 100 kW demand, that is $1,675 extra charged in 2021. There are more than 300 schools in the HRZ territory.

SEC has no dispute with whether the amount was underpaid to IESO for many years, nor with the explanation of the Applicant that it arose out of a simple spreadsheet error, and was caught by Alectra during a reconciliation[7].

We note, by the way, that unlike some other Group 1 errors in the past, this is not a case in which one category of customers was overcharged, and another category was undercharged. This is a case where the Applicant undercharged customers for many years, and underpaid IESO, and has since had to pay up.

The question that the Board faces is: Who should pay for this error? The Applicant says that the customers should pay, retroactively, for an error made by the Applicant.

SEC does not agree. Central to the idea that independent business corporations operate monopoly distribution franchises is that those companies will operate those businesses in a careful and rigorous manner. Neither the customers nor the regulator can interfere in their day-to-day operations, and in fact LDC's are quick to cry foul if the regulator seeks to "micromanage" their business.

That does not mean that the utilities are expected to operate without mistakes. Everyone makes mistakes, including utilities. While LDCs are expected to operate with a minimum of mistakes (it is in essence their core competency – operational excellence), no-one is perfect, and it would be unreasonable to expect them to be perfect.

On the other hand, it is not unreasonable to expect utilities to bear the risk of their own mistakes, which are entirely within their control, and outside of the control of the customers. LDCs get an ROE, which explicitly includes a substantial amount for business risk, because they are operating a business. Just like any other business, if they find an error after they have sold their product or service, they cannot go back to those who have purchased the product or service and retroactively increase the price. Errors are part of the risk that the business bears.

SEC therefore submits that the $8.1 million claimed by the Applicant arising out of this error should not be recoverable from customers. In this regard, it is important to distinguish between the $4.0 million relating to years cleared on a final basis, and the remaining two years:

1. ***Final Clearance - Years 2011-2016.*** With respect to the years 2011-2016, SEC submits that charging customers for the errors relative to these years is impermissible as retroactive ratemaking. Those customers not only paid for their distribution services in those years, but had no notice (through interim rates or otherwise) that the prices they paid could be changed in the future. There is no

[7] VECC-8, p. 2.

exception to the retroactive ratemaking rule that would be applicable here, and no new exception should be created.

2. ***Interim or No Clearance - Years 2017-2018.*** For 2017, the Applicant has cleared balances on an interim basis, and for 2018 they have not been cleared. Thus, the formal rule against retroactive ratemaking may not be applicable. That having been said, the Applicant is still seeking to have customers in 2021 pay for impact of the Applicant's error in 2017 and 2018. SEC believes that it is not appropriate to reach back several years to increase rates in these circumstances[8].

SEC therefore submits that the cost of Horizon's operational error ten years ago should be borne by the utility, not by the customers.

Horizon ESM Calculations and Allocations Generally

The Applicant takes the position that the earnings in the HRZ were below the threshold for earnings sharing, and so no amount should be shared[9].

SEC has two concerns about the Applicant's evidence:

1. ***Increase in Net Fixed Assets.*** The net fixed assets in the HRZ have increased in 2019 by $42 million, and were higher relative to forecast by $23 million[10]. By itself, this change results in the ROE decreasing by almost 90 basis points, and thus moving from above the threshold to below.

2. ***Opaque Allocations.*** The Applicant made a determination to integrate the accounting of the various rate zones, with a result that it is no longer able to identify the actual costs associated with the HRZ. Instead, allocation methods are used. The Board has accepted that allocations are appropriate, although expressing concern that the fairness of the allocations needs to be monitored[11].

On the first concern, SEC is not convinced that the increase in net fixed assets has been explained or justified[12]. The explanations are generic at best. Also, part of the

[8] The Board will be aware of the changes to the OEB Act in 2003 (c.3 in that year) that added subsections 32 (4.1) to (4.5) applicable to natural gas distributors, and subsections 78 (6.1) to (6.6) applicable to electricity distributors. That legislative change arose out of a similar situation, in that case a three year delay by a gas distributor in clearing flow-through deferral accounts, which produced large retroactive bills for many customers, including schools. While those provisions may not be directly applicable to years 2017 and 2018 in this case, the policy underlying those provisions is the same. Customers should not be getting a big additional bill, out of the blue, whether because of regulatory delay, or because of an error.

[9] Ex. 3/1/2, p. 2.

[10] Ex. 3/1/2, p. 6.

[11] EB-2019-0018, Decision with Reasons, pp. 38-39, dealing specifically with capitalization impacts, but having general application to allocations.

[12] See SEC-15 and, with respect to overall General Plant, SEC-19.

explanation is allocations, which leads directly into the second and more significant concern.

With respect to the second concern, SEC has sought to understand how the various allocation methods – for OM&A, for capital expenditures and capital additions, for capitalized overheads, etc. – were selected, and whether they are fair methodologies. We have been unable to do so on the evidence before the Board[13].

What we have found is that the allocation methods proposed appear to be reasonable on their face. They use objective information that has a plausible relationship to the amounts being allocated. They do not appear to be overly susceptible to manipulation, i.e. they are not inherently arbitrary. This all suggests that the allocations are OK.

On the other hand, the Board has no information on the results if different allocation methods are used, and has no way to model those different methods to make that determination. It is fair to assume that, in determining how to allocate, the Applicant tried several allocation methods for each category to be allocated, before alighting on the one to propose. It is also fair to assume, without in any way alleging impropriety, that the Applicant would select the allocation method that optimizes their position, for example by maximizing their revenue and therefore their profits.

The Board is thus faced with approving allocations in a vacuum, without full information with which to judge the fairness relative to the alternatives.

Given that the Applicant still has several years of IRM left, and the allocations can have a material impact on not just the ESM, but also the ICM thresholds, the capitalization of overheads, and the rates for the customers in each rate zone, SEC submits that the Board needs additional information to ensure that rates are just and reasonable.

The Board could order a comparison of allocation methods (for example, in the Applicant's next rate application), or even disclosure of the internal modelling done by the utility before selecting the final allocation method. This would result in the allocations being tested in an open forum, a rate case.

An alternative, which may be more efficient, is for the Board to order that OEB Staff conduct an external review of allocations by Alectra between rate zones, and report back (publicly) to the Board on the results of that review. That would include analysis of the impacts of alternative allocation methods.

[13] See, e.g. G-Staff-4, -6, and -7.

ICM Claims – Brampton

Two claims are made with respect to the BRZ: the CCRA true-up, and the first phase of the Goreway Road Widening[14].

Overall Capital Budget. SEC's general concern with respect to the BRZ is the overall increase in the capital budget. The average of the last three years' actuals is $27.6 million[15], well below the ICM threshold. The Applicant proposes to increase spending in the BRZ from past averages by about 53% to $42.2 million, and continue at roughly that level for several years. Of that increase, $8.4 million is in System Renewal[16], a 63% increase, and $7.9 million is in System Access[17], a 149% increase. There is a small offset due to a reduction in System Service expenditures, and a small increase due to General Plant, which includes the CCRA payment.

SEC has been unable to find in the evidence a cogent explanation for these increases. A project listing has been provided[18], but of the total of $42.2 million, $17.2 million is Miscellaneous projects, and $5.5 million is an allocation of General Plant (see earlier comments). There is no justification, for example, for a 63% increase in System Renewal capital spending in 2021 relative to prior year averages. This contrasts with the $16.1 million **reduction** in System Renewal capital spending by the Applicant across all of its service territory, relative to its DSP[19].

SEC submits that a utility should not be able to simply increase its capital spending to above the ICM threshold, then say "We need more money". That is especially true where, as here, the overall road authority budget across the Applicant's service territory is going down substantially in 2021 relative to prior years[20].

SEC therefore submits that, in this situation, the capital budget should be treated as the average of 2017-2019 actuals, plus the ICM projects, and then compared to the ICM threshold as ordinarily calculated. This would reduce the eligible capital for ICM purposes to about $3.9 million.

CCRA True-up. SEC has expressed its concerns in the past about the forecasting issues that lead to CCRA true-ups, particularly in the case of Brampton, which was part

[14] This is a three year project, with a net cost after contributions of $5.1 million over those three years: SEC-9. The Applicant indicates they may seek ICM treatment of the second and third phases.
[15] AMPCO-2, Table 1, 2017-2019. This appears to include a 2018 true-up for Pleasant TS, also in BRZ.
[16] Increase from a $13.4 million average to $21.9 million in 2021.
[17] Increase from a $5.3 million average to $13.2 million in 2021. It is not clear how much of this is net, because System Access projects typically include capital contributions from developers and others.
[18] Ex. 4/1/1, Attach 4.
[19] AMPCO-1(b), Attach 1. The same evidence shows that Alectra's System Access capex in 2021 is lower than its DSP, but by a smaller amount. In BRZ, the Applicant proposes big increases in both.
[20] AMPCO-2.

of Hydro One at the time the agreement in this case was negotiated. We are particularly concerned with the fact that the parties to the CCRA agreement did not forecast declining average use[21], when at that time (2008) it was clear that conservation programs were intended to do exactly that[22].

That having been said, SEC believes that the Board has not accepted those arguments in the past, and without those arguments a proper CCRA true-up should be recoverable from customers as an ICM claim (subject to being above the ICM threshold, of course).

In this case, however, there is no true-up to record. The Applicant has made clear that they have not agreed on the amount of the true-up with Hydro One, and they are merely estimating what they think it might be[23].

In this case, SEC submits that the ICM request for the true-up is premature. When the Applicant completes the process, and has a real amount to present to the Board, that is the time to seek recovery. The fact that there is a future true-up at year 15 is not really relevant. The Applicant will have a correct number within the next several months, after completing negotiations with Hydro one. When that happens, the Applicant can seek ICM recovery.

Goreway Road Widening. While the impact of the first phase of this project is not, in our view, sufficiently material to the operations of the Applicant to warrant an ICM application, it is part of a larger project[24], and that is arguably material. The incremental revenue requirement of about $118,000[25] is an easily manageable amount in the context of a utility of this size, but the overall net capital cost is $5.1 million over all three years.

SEC therefore does not object to inclusion of this project, assuming it comes within the ICM threshold.

ICM Claim - Powerstream

The Rutherford Road Widening project is the only ICM claim for the PRZ. The claim of $2.9 million relates to the third and last phase of a project with a total net cost of $8.2 million. The previous phases were not the subject of ICM claims[26].

[21] 1-BOMA-3.
[22] On these issues we have had an opportunity to see the submissions of VECC, and we largely concur with their analysis.
[23] BRZ-Staff-21.
[24] SEC-9.
[25] Ex. 2/1/1, p. 10 has the total ICM impact, but not a breakdown. We have estimated the impact of this project using the same ratio as the $2.1/$2.9 million ratio of cost for the Goreway and Rutherford Road Widening projects.
[26] SEC-13.

There do not appear to be any issues with the calculation of the ICM threshold for the PRZ[27], and this project is of a type that the Board has in the past allowed ICM recovery.

The only problem with this is that the actual impact on the Applicant's costs is $162,795 per year[28], and while the Applicant says that is material, we are unable to see how that could be true. Just as the previous two phases were managed within the Applicant's capital budget for the PRZ, it would seem self-evident that this phase could be handled just as easily.

SEC therefore submits that ICM recovery of this project should not be approved.

Effective Date

It may be that the Board's decision in this proceeding arises quickly, and as a result new rates can be implemented by January 1, 2021. However, if that is not the case, SEC submits that the effective date for any rate increases arising out of this Application should be the beginning of the month following the Board's decision, and any revenue shortfall in the interim period should be for account of the Applicant, not the customers.

In this regard, SEC asked the Applicant to provide justification for the timing of the Application[29]. In our view, the justifications offered are not sufficient to allow recovery of revenue shortfalls for the period from January 1st until the date new rates are in place.

A truly mechanistic IRM application, if filed in August, could be implemented by the end of December. The Board does that regularly.

In this case, the Applicant knew that, in addition to the normal components of an IRM application, it would have at least three different ICM claims, plus an ESM, plus a material retroactive adjustment for an error, all of which had the potential to be controversial. In fact, on May 20, 2020 it reported to its Board committee on this Application, and the components of it[30], so it appears that it could have filed much earlier.

SEC is conscious that covid-19 has caused delay in many aspects of utility regulatory activities, and utilities like the Applicant may seek to have the customers bear 100% of the costs of those delays. In this case, however, the delay appears to be that the Applicant simply aimed for the end of August, hoping for a fast turnaround despite the complexity of the Application.

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[27] Subject of course to the allocation issues discussed earlier, which permeate all such calculations.
[28] Ex. 2/1/1, p. 17.
[29] SEC-1.
[30] CCC-2, Attach 2. Interestingly, in both that report, and the report dated August 19th, management said that it was unsure whether it would apply for an ICM. In fact, the actual Application had already been filed on the latter date, with ICM claims included.

Despite the fact that the Board has processed this Application very quickly, there is a chance that new rates will not be in place by January 1st. If that is the case, SEC submits that any foregone revenue should not be recovered from the customers.

Summary of SEC Recommendations

SEC therefore submits:

1. ***2010 Global Adjustment Error.*** This amount should not be recoverable from customers, as it is retroactive ratemaking arising out of a utility error. In the alternative, the $4.0 million that relates to years cleared on a final basis should not be recovered from customers.

2. ***HRZ ESM and Other Allocation Issues.*** The Board should order an external review by OEB Staff of the allocations between rate zones by the Applicant, including those relating to OM&A, capital expenditures/additions, and capitalized overheads.

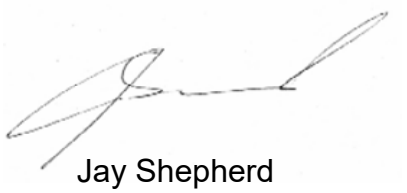
3. ***ICM Brampton.*** The amount of capital in excess of the ICM threshold should be reduced to $3.9 million, consistent with past capital spending. The CCRA true-up is premature, and should not be approved. The Goreway Road Widening should be approved to the extent that it exceeds the revised ICM threshold.

4. ***ICM Powerstream.*** The ICM claim should not be approved, as it does not have a material impact on the Applicant's costs.

5. ***Effective Date.*** Any rate increases should be effective at the beginning of the month following the Board's decision, and any foregone revenue should not be recoverable from customers.

All of which is respectfully submitted.

Yours very truly,
SHEPHERD RUBENSTEIN
PROFESSIONAL CORPORATION



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cc: Wayne McNally, SEC (email)
Interested Parties