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January 25, 2021

Ms. Christine Long
Registrar
Ontario Energy Board
2300 Yonge Street
Suite 2700
Toronto, Ontario, M4P 1E4

Dear Ms. Long,

RE: EB-2020-0133 - London Property Management Association – Written Comments on the Staff Proposal – Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency

1. INTRODUCTION

The following are the comments of the London Property Management Association ("LPMA") on the OEB Staff Proposal ("Staff Proposal") in the Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency dated December 16, 2020.

On March 17, 2020, the Ontario Government declared a state of emergency in response to the spread of COVID-19. One week later the Ontario Energy Board ("OEB" or "Board") established a deferral account ("Account") in which electricity and natural gas distributors may record incremental costs as a result of the ongoing COVID-19 emergency. In April, 2020, the Board confirmed the applicability of the Account to electricity transmitters and Ontario Power Generation ("OPG").

The comments that follow also take into account the expert reports from London Economics International LLC ("LEI") that were commissioned by the OEB to support the Deferral Account Consultation ("Consultation"). In particular, LPMA has reviewed each of the four following reports from LEI:

- COVID-19 Impact Study
- A Report on Regulatory Principles, Policies and Accounting Treatments Applied in Other Jurisdictions in Response to COVID-19
- A Report on Gains and Losses from Differences in Load and Production, and

- A Report on the OEB's Cost of Capital Parameters and the Impacts of Covid-19.

The comments that are provided below are presented in the same general format and order as sections 3 through 6 of the Staff Proposal. Section 2 of these comments deals with the necessity of financial viability. LPMA has also added a Section 7 that deals with issues that appear to be absent from the Staff Proposal.

While the proposals provided by Board Staff ("Staff") are a step in the right direction, LPMA believes that they do not go far enough in ensuring that ratepayers will only be required to provide financial support to ensure the financial viability of their utility.

The Staff Proposal envisions a 50/50 sharing of net costs (and 100% recovery of costs necessary to comply with government and OEB actions aimed at providing relief to ratepayers in response to the pandemic) for those utilities have a return on equity ("ROE") that is no greater than the lower end of the dead band of 300 bps from a utility's approved ROE. Staff also suggest that limiting any recoveries up to the lower end of the dead band is an important element to avoid the potential that utilities that underearn end up in a better financial position, after having their claims approved, than those operating within the dead band, all else equal.

LPMA submits that there appears to be a dichotomy in the Staff Proposal. On one hand, the purpose of the Account is to ensure the financial viability of the utility, while on the other hand the 50/50 sharing of some net costs and the 100% recovery of other costs appear to be totally independent of the financial viability of the utility.

While the Staff Proposal indicates that where utilities pass the means test, but can demonstrate that their financial viability would be compromised if their pandemic-related recoveries are limited to the 50% of some net costs, the OEB should consider recoveries at a rate greater than 50% on a case-by-case basis it is silent on the opposite scenario.

A utility may be financially viable without recovering 50% of some net costs and 100% of other costs. In fact, a utility may be financially viable without the recovery of any costs. Clearly there is no direct or demonstrable link between a percentage recovery of costs and financial viability.

LPMA does not believe that any ratepayer money associated with increased costs or lost revenues related to the COVID-19 emergency should be used to simply enhance the bottom line for the benefit of shareholders that are already earning a positive return on equity and have not taken all the steps that they should to ensure their own financial viability. As an example, take a utility that has a 9% approved ROE built into rates and its actual ROE for 2020 is 5%. It passes the means test because the ROE is less than 300

bps below the approved ROE (6%). Regardless of the amount it is allowed to recover from ratepayers through the Account (capped at an amount that would increase the ROE to 6%) all of this ratepayer money goes directly to the bottom line and ultimately to the shareholder. The OEB would need to ask itself if it is just and reasonable as a result of a pandemic to enhance the profitability of an already profitable utility at the expense of ratepayers that have suffered much more than the utility shareholders. In the example, does a utility need a ROE of something in excess of 5% to remain financially viable?

LPMA notes that Staff refer to a "financial need", "financial health" and "financial hardship" several times within the Staff Proposal. LPMA submits that these references are not equivalent to "financial viability" and should not be interpreted as such. For example a company can be experiencing financial hardship while maintain its financial viability.

2. THE NECESSITY OF FINANCIAL VIABILITY

LPMA supports the principle of necessity, which underpins the Staff Proposal and is defined as:

> "Recovery of any balances recorded in the Account should be subject to evidence that the costs are not only reasonable, but also necessary to the maintenance of the utility's financial viability".

LPMA believes because of the importance of the concept of "financial viability" in the Staff Proposal and in its own comments, there should be an agreed upon definition of the phrase. LPMA defines "financial viability" as the ability for an entity such as a utility to achieve its operating objectives and fulfill its mission over the long term.

LPMA submits that the only credible reason for the existence of the Account for electricity and natural gas utilities (including OPG) is the need to ensure that these providers of essential services remain financially viable to serve their customers.

Regulation of the utilities is needed to serve as a proxy for competition. In competitive sectors of the economy, many businesses have incurred, and continue to incur, reduced profitability due to the pandemic. Many are not profitable or even breaking even. Many have incurred and continue to incur losses and thousands upon thousands have closed.

The federal, provincial and municipal governments have all provided support to business and individuals in unprecedented ways, ranging from wage support programs to reduced electricity rates to loans and grants to businesses and to the deferral of payment of property taxes. The cost of these programs is significant but have been deemed appropriate to support the economy.

Many of these programs have requirements that need to be met in order for a business to qualify, such as a minimum reduction in revenue from one period to another. In other words, the governments have decided that some businesses need support, while others do not.

Regulated utilities may not qualify for many of these programs, although they do qualify for others (most likely some of the smaller utilities that may be impacted by the loss or reduction in consumption associated with a small number of large customers).

LPMA asks the question, should the Board provide protection beyond what the governments have deemed is appropriate, and if yes, what is the magnitude of this additional protection?

LPMA submits that the answer is that, yes, the Board should provide protection beyond what the governments have deemed is appropriate. This is because, unlike most other businesses, regulated utilities provide an essential service and they cannot simply shut down. The closure of a restaurant, retail store, hair salon or any other business deemed to be non-essential due to a lack of financial viability has an impact on a limited number of people. These businesses operate in a competitive environment and there will be many that provide the same services and remain financially viable during the pandemic.

As to the magnitude of the additional protection provided by the Board through the Account, LPMA submits that any recovery mechanism that provides more than what is needed to maintain financial viability would be misaligned with the Board's role to mimic competitive forces. To provide any amounts in addition to what is required to maintain financial viability is simply a transfer from ratepayers (individuals and businesses) to the bottom line for the benefit of shareholders that are already making a profit.

People and businesses (including their owners) are suffering not only financially but emotionally. People have lost jobs as businesses have closed and do not know where, or when, they can get a job. Businesses that have not closed yet, fear for their future, as do their employees. The OEB would have to take a good long look at itself in the mirror if it were to allow utilities to recover amounts from these ratepayers that are not required to ensure the financial viability of the utilities. Not only would it be making the financial suffering worse through higher rates to recover this unnecessary amount, but it would also reduce hope for business that survive the pandemic only to be hit with higher costs.

LPMA submits that the Board should also embrace the principle of non-necessity.
LPMA defines this principle as:

> "Recovery of any balances recorded in the Account in excess of the minimum amount required to maintain a utility's "financial viability" is not required and will not be permitted."

3. OVERVIEW OF THE PANDEMIC'S IMPACT ON THE SECTOR, THE ECONOMY AS WHOLE AND ON RATEPAYERS

Staff noted that the pandemic crisis has resulted in far-reaching economic and societal impacts across Ontario. Staff further noted that that utilities, as providers of essential services, have appeared to have fared better financially relative to other businesses. LEI also noted in its *Covid-19 Impact Study* that Ontario's seasonally adjusted real gross domestic product ("GDP") change by industry for the second quarter of 2020 showed that declines in real GDP for the utility sector were less significant relative to all other industries, with the exception of finance and insurance. Based on the second quarter data, the decline for the utilities sector was 1.3%. For comparison purposes the total production (i.e. output across all industries) was a decline of 12.4%. The table was produced by LEI and was reproduced in the Staff Proposal in Figure 10.

LPMA has updated this table to reflect data that is now available for the third quarter of 2020 and has been included in Appendix 1 to these comments. The source of the data is the same as that used by LEI with the exception that the data has been updated to reflect data from the third quarter of 2020 that was not yet available to LEI at the time of the preparation of their report.

The figures shown in the table show the real GDP change between the third quarter of 2020 relative to the first quarter of 2020. Only two industries – real estate, rental & leasing and finance and insurance – have posted growth over this period. Utilities have recovered much of the loss recorded in the second quarter of 2020 (1.3% as shown in Figure 10 in the Staff Proposal) with a decline of only 0.4% through the third quarter of 2020. Similarly, the decline in total production – the output across all industries – has fallen from 12.4% (Figure 10 in the Staff Proposal) to 3.4%. In fact, a comparison of the figures shown in Appendix 1 to those in Figure 10 show that real GDP has rebounded in the third quarter relative to the second quarter.

Based on the second quarter 2020 real GDP figures, LEI concluded that the industry assessment showed that, at a time when the impact of the pandemic resulted in the largest quarterly real GDP decline on record, the impact in the utilities industry was not particularly severe (with a decline of 1.3%). LPMA submits that based on the updated information for the third quarter 2020 real GDP figures, the recovery has also been significant, as reflected in the reduction in total production of 12.4% in the second quarter

of 2020 relative to the first quarter of 2020, to a decline of 3.4% in the third quarter of 2020, also relative to the first quarter of 2020.

LPMA also notes that the utilities industry has continued to fare much better than most other industries and the reduction in real GDP stands at only 0.4% in the third quarter of 2020, relative to the first quarter of 2020. This confirms and reinforces LEI's conclusion that the impact in the utilities industry was not particularly severe. LPMA also submits that the rebound in the third quarter for utilities also reflects that the impact in the utilities industry was not particularly long.

Appendix 2 to these comments shows the level and percentage change in the real GDP for the utilities industry over 55 quarters from 2007 through the 2020 (Q3) period. The source of this data is the same as for that found in Appendix 1. LPMA submits that this chart highlights a number of facts about the utility industry.

First, even though the pandemic has been described as a once-in-a-century crisis, its' impact on the utility industry is far from a once-in-a-century event. In fact, based on the reduction of 1.9% in 2020 Q2, this reduction is only tied for the 12th worse in the last 55 quarters since the beginning of 2007. Three of these quarterly declines exceeded 5%.

Second, the pandemic related downturn lasted only for 1 quarter. Over the last 14 years, the utility industry has recorded downturns that last more than 1 quarter on 7 occasions. Four of these declines have lasted more than 2 quarters.

Third, the utilities industry was already in the midst of one of these extended declines before the pandemic occurred. As shown n Appendix 2, real GDP in the industry declined by 3.9% in 2019 Q4 and a further 1.0% in 2020 Q1. In aggregate, this pre-pandemic decline of 4.9% is 1.7 times the decline experienced in the pandemic impacted 2020 Q2.

Fourth, the reduction in economic activity for the utilities industry in the current pandemic is a fraction of the impact on the industry that took place as part of the 2008-2009 recession. As seen in Appendix 2, the impact of the in the second and third quarters of 2020 is a net decrease of 0.3%. The decline in the industry in the fourth quarter of 2008 through the third quarter of 2009 was a cumulative decline of 6.4% as a result of four consecutive declines of 1.2%, 0.8%, 2.4% and 2.0%. LPMA submits that there is clearly a significant difference on the utilities industry between the 2008/2009 recession as compared to the impact of the pandemic. Not only did the 2008/20-09 recession impact the utilities industry for a longer sustained period, it resulted in real GDP output for the industry to decline more than 20 times more than in the current pandemic.

Staff and LEI have provided more information on the provincial utilities.

In its independent report titled *A Report on the OEB's Cost of Capital Parameters and the impacts of Covid-19*, LEI's findings suggest that the utilities in Ontario appear to be fairly compensated for their risks based on current parameters. In the same report, LEI noted that over the pre-covid period from 2010 through 2019, the Ratio of Ontario allowed ROE to the S&P 500 return was 95.8% (Figure 6). In the post-covid period for 2020, this ratio has increased to 120.3%. LPMA submits that this is another indication that the utilities industry has been less impacted by the pandemic than the economy in general.

Staff indicates that it has been collecting data from electricity distributors on a monthly basis with respect to their cash flow and states that the distributors have generally managed well during the pandemic to date. Staff also noted that there does not appear to be any immediate liquidity issues for the electricity distributors at this time.

In its September 24, 2020 letter re *Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency – Next Steps*, the Board stated that in addition to reviewing the Account balances reported by utilities, that it was continuing to monitor the impact of COVID-19 on the financial health of utilities based on their monthly reporting to the OEB. At that time the Board stated that this reporting had not identified any acute financial issues for utilities. Further, the Board noted that any individual utility that anticipates financial or operational viability issues should contact the OEB immediately to discuss their specific circumstances. LPMA is not aware of any utility contacting the OEB or requesting any relief to date. If there have been any such requests, the Board should ensure transparency of any such request or correspondence and make that information public to ensure regulatory efficiency and a timely review.

At the time of its creation by the Board, the impacts of the Ontario Government's declaration of a state of emergency and the repercussions on the economy and in particular, on the utilities industry, was not known and highly speculative. In light of the unknown impacts and the potential magnitude of the impacts, the creation of the Account was justified. Based on updated information now available, as described above, the need for the Account, in the view of LPMA, has been substantially reduced.

In the sections that follow, LPMA provides its comments on the Approach to Staff Proposed Positions, Staff Proposed Positions and Disposition Matters sections of the Staff Proposal. LPMA has included its recommendations where it disagrees with the Staff proposals or where it believes the proposals need to altered, changed or expanded.

4. APPROACH TO STAFF PROPOSED POSITIONS

4.1 Overall Approach

LPMA submits that the approach outlined by the positions in the Staff Proposal are not consistent with the principle of necessity. While LPMA strongly supports the principle of necessity and believes that it is the only grounds on which a utility should be allowed to recover net incremental costs (i.e. in order to maintain financial viability), the positions outlined in the Staff Proposal for what should be included in the Account are for the most part, irrelevant.

Much of the Staff Proposal deals with what should go into the Account and then arbitrarily allocates the amounts in the Account on a 50/50 basis except in cases where a utility can provide an indication of financial hardship or other extenuating circumstances where they may need more than 50% of the balance in the Account. This entire approach ignores the bigger picture, that of the need for ensure the financial viability of each utility.

Would the Board allow a utility to only collect 100% of the balance in the Account if that amount was not sufficient to ensure the viability of the utility? LPMA would hope not. Would the Board allow a utility to collect 50% of the balance in the Account if that amount was more than sufficient to ensure the viability of the utility? LPMA again would hope not. This exercise should not be about throwing money away; it should be about ensuring the financial viability of each utility while minimizing the impact on ratepayers.

LPMA sees the amount included in the Account for those utilities that pass the means test – whatever that may end up being – as only a guidepost of the potential impact on the magnitude of the amount to be paid by ratepayers. Similarly, the arbitrary 50% is only a another signpost along the way. The destination of the exercise is the necessity to maintain a utility's financial viability. How we get there is not as important as arriving at the right destination.

4.2 OEB's Role and Principles

In Section 2 above, LPMA indicated its strong support for the principle of necessity as defined by Staff.

Staff have recommended that the recovery of the Account balance requires each of the following:

- A preservation of the financial incentives inherent in, and consistent with, the OEB's general incentive ratemaking framework,
- A recognition of the fact that both customers and utilities are adversely impacted from the same events, and
- A need to demonstrate that earnings are beyond the rage of reasonably expected fluctuations for a regulated utility.

LPMA submits that the first point noted above is achieved by the necessity principle in that it maintains the financial viability of a utility, which matches the Board's objective of the maintenance of financially viable electricity and natural gas industries while protecting the interests of consumers with respect to prices.

The second bullet point is reflected in the need for regulation to serve as a proxy for competition. If a utility is financially viable without recovering any of the net incremental costs incurred, then it should not receive any special treatment, as special treatment is not available to competitive industries. The federal and provincial governments have established numerous programs to assist businesses during the pandemic. Some businesses qualify and some do not, depending on their situation. Utilities should be treated the same way. The necessity principle comes into play and provides special treatment to utilities that can demonstrate that their financial viability is threatened as a result of the pandemic. The reason for this special treatment is clear: utilities provide an essential service and cannot be allowed to fail. In a competitive market, companies can and do fail.

LPMA takes issue with the third bullet point. It is not consistent with the principle of necessity. Staff appear to be of the view that if earnings are beyond the range of reasonably expected fluctuations for a regulated utility (i.e. the +/- 300 bps dead band), and in particular, if the earnings are below the lower end of this dead band, then the financial viability of the utility is not maintained. LPMA strongly disagrees.

There is nothing to indicate that a utility cannot maintain its financial viability if its ROE falls to 300 bps below the Board approved level embedded in rates. In fact, if this were the case, then Ontario is currently full of utilities that are not financially viable before the pandemic occurred. As noted in Section 5.4.2 below, many utilities have under earned by more than 300 basis points and no action has been taken by the Board to maintained their financial viability. In fact, the utilities themselves have not sought Board assistance to maintain their financial viability. These utilities have remained financially viable without any assistance from the Board or ratepayers despite having earnings below the bottom level of the dead band. Clearly earnings below the bottom level of the dead band do not necessarily mean that financial viability is in jeopardy.

LPMA submits that an ROE falling below 300 basis points from that embedded in rates is a necessary condition to be concerned about the financial viability of a utility. However, it is not sufficient to determine that the financial viability of the utility is jeopardized.

4.3 Examination of Existing OEB Policy

4.3.1 Z-Factor

LPMA's comments related to the applicability of a Z-factor to the pandemic and to lost revenues and bad debt, in particular, are provided below in Sections 5.5.2 and 5.5.4, respectively.

LPMA agrees with the Staff position that the pandemic should not be considered directly comparable with other unforeseeable events, such as Z-factor events. However, the reasons for this position are a little different from that provided by Staff.

The impact of the pandemic is not directly on utilities. It is an indirect impact on utilities because the pandemic has had an impact on the economy. In this case, the pandemic is no different than the dotcom bubble, a trade war, runaway inflation or energy prices or anything else that can and has impacted the economy and driven it into a recession or a near-recession. The impact on the economy is not specific to the utilities industry. It has impacts across all sectors, with some sectors being hit hard and with others doing relatively well (See Appendix 1 and comments related to Appendix 1 in Section 3 above).

These economic conditions are being reflected throughout the economy in such things as inflation and interest rates. These are economy wide factors that impact all sectors of the economy and are not specific to utilities, anymore than are lost revenues, increased bad debt and increased costs for PPE. Unlike many sectors of the economy, utilities have not been required to shut down. As a result the brunt of the impact of the current economic situation is being felt not by the utilities but by their customers.

4.3.2 Means Tests – ACM/ICM, Inflation Pressures, Off-Ramps

LPMA strongly supports the approach of a means test for utilities to qualify for the transfer of any amounts from ratepayers to utilities. A test should be applied to utilities to demonstrate that they require the transfer of some amount from ratepayers in order to maintain their financial viability. LPMA supports a multi-pronged approach to the means test. Details are provided under Section 5.4.2 below.

5. STAFF PROPOSED POSITIONS

5.1 Criteria for Recording Amounts

5.1.1. Approach

Staff identify two approaches in articulating what types of impacts may be recorded in the Account for utilities that expect to meet the means test: a prescriptive approach that specifies what kinds of incremental impacts may be recorded; and a flexible approach that allows the utility to record what it has deemed to be a discrete, incremental impact and directly attributable to the pandemic.

LPMA agrees with the Staff that the flexible approach is more appropriate, given the diversity in size, operation and customer makeup in the utility industry in Ontario. A one size fits all approach does not appear to be appropriate given that the impacts of the pandemic vary by region to region and customer type to customer type.

While supporting the flexible approach, LPMA has the following observations. First, the flexible approach will have less certainty and predictability of the amounts that are brought forward for disposition than would the prescriptive approach. This is the price for flexibility.

Second, LPMA submits that under a flexible approach, utilities should not be the only ones that deem what is a discrete, incremental impact and directly attributable to the pandemic. Ratepayers and Board should also have the ability to bring forward such impacts for review. Utilities should be required to provide such information where requested as part of any disposition application.

5.1.2 Causation, Prudence and Materiality Criteria

Causation

LPMA agrees that the impacts recorded must be determined to have only been incurred as a result of the pandemic.

LPMA further submits that the amounts recorded in the Account should be at the same level of detail as an appropriate baseline for the costs to ensure that any incremental impact measurement can be established. This incremental impact measurement should also take into consideration the advancement of costs from future years. For example, if a utility invested in additional laptops or other IT infrastructure to allow employees to

work from home, it would be expected that future laptop replacements and other IT infrastructure spending may be reduced.

Prudence

LPMA agrees that all amounts recorded in the Account must be prudently incurred. The utility must be able to demonstrate that it has acted prudently to minimize those impacts and has fully availed itself of all available cost reductions and savings, including those that have become available as a result of the pandemic.

LPMA submits that the criteria of prudence should go even farther than this because the need for the Account is to ensure financial viability of the utility. The utility should be required to show that it has taken all steps necessary to protect its financial viability. A utility is required to, and is compensated for, providing an essential service in a safe, reliable and cost-effective manner. If the financial viability of a utility is in question, it may not be able to maintain safety, reliability and cost-effectiveness at the same time.

As part of any application to recover any amounts in the Account, LPMA submits that utilities should be required to file their emergency preparedness plans that were in place at the beginning of 2020. They should also be required to demonstrated that those plans were followed and implemented quickly.

Utilities should also explain how changes in their planning processes and business plans were carried out in demonstrating prudence in the face of the pandemic.

Materiality

LPMA does not agree with the Staff recommendation that the standard materiality threshold should apply if the Board determines that the need for the Account is restricted to ensuring the financial viability of a utility.

If a utility is financially viable without the recovery of any amounts in the Account, it should not recover any of those amounts and materiality is irrelevant.

If a utility is not financially viable without the recovery of at least some of the amounts in the Account, it should only recover the amounts necessary to maintain its financial viability. This amount could be over or under the materiality threshold.

Denying the recovery of an amount deemed not to be material for a utility that needs that amount to maintain financial viability would be an imprudent decision by the Board, as

would the recovery of any amounts in the Account because it is deemed material, but not all of which is required to maintain financial viability.

Staff has recommended that the materiality threshold should be applied to the total amount recorded in the Account and not on a sub-account basis. While LPMA believes that the materiality threshold is not needed if financial viability is the basis for recovery, if the Board were to determine that some other driver determines the amount recovered through the Account, the LPMA submits that the Staff recommendation to use the total amount recorded in the account is appropriate.

Staff recommends that there should be one exception to their rule. Staff suggest that costs associated with complying with government or OEB actions designed to assist ratepayers should be assessed separately from the other costs in the Account.

LPMA does not agree with this proposal. Again, based on the need for the Account to ensure financial viability of the utilities, there is no need for separate treatment of any costs. All the costs (and savings) should be aggregated into one amount. Utilities that demonstrate a loss of financial viability should then be eligible to recover an amount to ensure their financial viability – regardless of the source of the impact – up to the maximum amount in the Account. Similarly, the costs that Staff suggest should be assessed separately should not be recoverable if their recovery is not required to ensure financial viability.

5.1.3 Costs, Savings and Netting Treatment

LPMA agrees that the Account should track both increases and decreases in costs. It does not, however, believe that lost revenue from reduced load should be tracked in the Account. This position is detailed in Section 5.5.2 below.

If the Board were to determine that the impact of lost load should be included in the Account, then LPMA submits that all of the associated impacts should be included, ranging from the loss of distribution revenue, to the reduction in working capital allowance (cost of power makes up 90% or more of the working capital allowance for many utilities), to the reduction in operating and maintenance costs because of lower demands on the equipment, to a potential for lower line losses.

5.2 Measuring Incremental Impacts

The Staff Proposal sets out a mathematical approach to define incrementality of both costs and savings. The proposed methodology is set out on page 17 of the Staff Proposal and LPMA will not reproduce the methodology here.

LPMA supports the concept that is included in the Staff Proposal but has two specific changes that it believes should be made.

The Staff Proposal notes that the amount embedded in rates should be adjusted for inflationary increases less productivity. LPMA supports this adjustment as it provides a starting point for a reasonable proxy for costs in 2020 or for whichever year balances in the Account accrue. However, the Staff Proposal is silent on an adjustment to the second part of the baseline, that being the highest actual annual amount over the past five years (2015 to 2019).

First, with respect to the adjustment to the amounts in embedded in base rates (and as noted below embedded in actual costs in 2015 through 2019), LPMA submits that all OM&A related costs should also be adjusted to account for customer growth in addition to inflation less productivity.

It is well known that OM&A costs grow as the number of customers increases. This growth is over and above that attributed to inflation less productivity. It is well documented in the Pacific Economics Group ("PEG") Benchmarking Spreadsheet Forecast Model, which is used to determine the cost benchmarking results for electricity distributors. This model contains an adjustment factor or customer elasticity that is used in predicting costs for benchmarking purposes. This customer elasticity varies by distributor but is often in the neighbourhood of 0.45. This means that costs increase as the number of customers grows, although at less than a 1 to 1 ratio.

LPMA submits that the impact of customer growth between the amount embedded in base rates and in the actual annual amounts over the 2015 through 2019 period should be included in the adjustment to arrive at equivalent 2020 dollars by adding an "adjusted customer growth rate" to inflation less productivity. This "adjusted customer growth rate" would be equal to the annual percentage increase in the number of customers times the customer elasticity used by PEG in their Benchmarking Spreadsheet Forecast Model.

Second, with respect to the actual annual amounts for the 2015 through 2019 period, LPMA submits that each of the years should also be adjusted for inflationary increases less productivity plus adjusted customer growth to bring the costs in those years to an equivalent proxy for 2020 costs. Not doing so would effectively categorize inflation increases (less productivity) and adjusted customer growth as a COVID related increase, which is clearly not the case.

This adjustment to the 2015 through 2019 actual costs would be applicable to both incremental costs and incremental savings.

As noted above, the Staff Proposal for the second part of the baseline is to use the highest actual annual amount over the 2015 through 2019 period for incremental costs and the lowest actual annual amount over the 2105 through 2019 period for incremental savings. The Staff Proposal indicates that Staff also considered the five-year average of the historical results instead of the five-year high/low approach. The rationale for consideration of the five-year average is that the intent is to derive a reasonable baseline for 2020 without the pandemic occurring and that a five-year average would mitigate anomalies in a singular year.

LPMA submits that the Staff recommendation to use the high/low approach rather than a five-year average is appropriate. The intent of measuring incrementality as a result of the pandemic is to arrive at a reasonable estimate of the costs and savings that are directly attributable to the pandemic. There are as likely to be anomalies in 2020 that are unrelated to the pandemic as there were in each of 2015 through 2019. Using an average over this period would implicitly assign any non-pandemic anomalies as pandemic related.

Further, the use high/low approach for incremental costs/ savings reflects the impact of typical fluctuations in costs. The pandemic related incremental costs and savings should only be those beyond those typical fluctuations. Use of the five-year average approach eliminates these typical fluctuations, leaving it open to interpretation as to which portion of the incremental costs/savings are due to the pandemic and what proportion could be considered a typical fluctuation from one year to another.

Using the high/low approach means that any amount in 2020 that is higher/lower will be categorized as pandemic related incremental costs/savings. This is not likely to be the actual case, as actual costs for 2020 could be higher/lower than the adjusted levels in base rates and in 2015 through 2019 in the absence of the pandemic. However, LPMA submits that this approach provides a more reasonable approximation of the incremental pandemic related costs and savings than using the five-year average approach.

With respect to any emergency-related funding or government assistance, LPMA agrees with the Staff position and submits that any unallocated amount should be applied an offset to any pandemic costs incurred and this can be accomplished through a standalone entry in the Account.

Staff has identified a potential problem in identifying amounts included in base rates where a Board decision or an approved settlement agreement ordered a change to an OM&A envelope without any specific amounts being allocated to part of the envelope. Staff suggest that in this situation a utility should identify the amounts in base rates on a best-efforts basis and that, as an example, a utility could apply the percentage reduction

to the OM&A envelope approved by the Board or settled by the parties, to the utility's requested amount in the same proceeding.

LPMA submits that this is one option or methodology that could be used, but there may be other more appropriate approaches that could be utilized. LPMA believes that any methodology should be proposed by the utility and be determined on a case-by-case basis.

5.3 Net Cost Sharing

5.3.1 Recovery of Rate Eligible Amounts

The Staff Proposal would see utilities that pass a means test be able to recover 50% or more of the amounts recorded in the Account and 100% of the costs associated with the items shown on page 19 of the Staff Proposal. LPMA submits that neither of these two proposals for recovery is consistent with the principle of the necessity of maintaining financial viability.

With respect to the 50/50 sharing proposed for most of the net incremental costs, this is clearly an arbitrary sharing. Staff essentially say that it would not be appropriate to recover all costs from customers nor would it be not appropriate to fully disallow all costs from being recovered by utilities. The 50/50 proposed sharing is an attempt to split everything down the middle.

As noted earlier in this submission, the Staff Proposal defines the principle of necessity as:

> "Recovery of any balances recorded in the Account should be subject to evidence that the costs are not only reasonable, but also necessary to the maintenance of the utility's financial viability".

Clearly, in the view of LPMA, the recovery of an arbitrary percentage of the net incremental costs in the Account is not consistent with the principle of maintaining the utility's financial viability. Some utilities may require only 10% of the amounts recorded in the Account to maintain their financial viability. Others may require all of the amounts in the Account to remain financially viable.

LPMA notes that Staff have proposed that a utility may propose to recover more than 50% if they can prove an instance of financial hardship or other extenuating circumstances that suggest a 50/50 cost sharing that financial viability may be at risk. LPMA submits that the first dollar requested should be based on financial viability being at risk. Why should ratepayers be expected to automatically grant a utility 50% of the net

incremental costs if they cannot prove that they need at least this amount to maintain their financial viability? Many of the utilities that may pass the means test will still be earning a positive rate of return on their investments. Many businesses, small and large, are not in that enviable position. Their ROE is negative or irrelevant if they have closed down.

LPMA submits that the Board should determine the dollar - not a percentage – amount in the Account that is required to maintain financial viability of a utility on case-by-case basis. As LPMA has previously stated in these comments, the Board should also embrace the principle of non-necessity. LPMA defines this principle as:

> "Recovery of any balances recorded in the Account in excess of the minimum amount required to maintain a utility's "financial viability" is not required and will not be permitted."

Staff proposes to allow the recovery of 100% of the net incremental costs for the following items, as long as a utility is not over earning by more than 300 basis points:

- Implementation cost of emergency time-of-use rates and deferred global adjustment charges for electricity distributors
- Implementation and administration costs of CEAP and CEAP-SB
- Increased LEAP EFA funding
- Lost revenues from certain reduced/waived specific service charges and
- Incremental bad debt directly attributable to the extension of the winter disconnection ban.

LPMA does not agree with Staff that there should be separate treatment for the costs necessary to comply with government or Board actions aimed at providing rate relief to ratepayers in response to the pandemic. These costs should be treated in the same manner as other net incremental costs are and should be recoverable only to the extent needed to maintain financial viability.

The government and the Board have mandated actions aimed at providing relief to ratepayers in response to the pandemic. Recovery of the costs associated with these actions is like giving money to ratepayers with one hand and taking it away with the other. It makes no sense to LPMA why the government and the Board would allow special treatment for these costs and allow the utilities to recover 100% of these costs and not be subject to a means test to demonstrate that their financial viability is at risk without recovery.

LPMA further submits that it is a slap in the face of ratepayers, many of whom face significantly more dire circumstances than the utilities, to allow the utilities to recover these costs even if they are earning an ROE of up to 300 basis points over their allowed

rate of return! In effect Staff is proposing that ratepayers pay the costs of the government and Board mandated actions at providing relief to ratepayers in the pandemic directly to the shareholders bottom line, adding to their level of profitability.

LPMA submits that it is highly unlikely that the government would have expected ratepayers to pay for the costs associated with rate relief.

LPMA further submits that the regulator's role is to mirror the financial impacts that utilities would face if they were not operating as monopolies. In isolating these specific costs, Staff seem to assume that the government actions in the pandemic only affect regulated utilities and so they need special help.

The facts are that the actions of the government have impacted everyone. Retail stores, restaurants, bars, personal service provides and many others have been forced to close and were only allowed to do curbside pickup. Unlike utilities, the revenues of these businesses dropped to a fraction of the normal level.

The government imposed a moratorium of the eviction of residents and businesses for the non-payment of rent. These property owners, just like utilities, face mounting bad debt expenses. The entire supply chain the underpins industries throughout the economy face increasing bad debts as their clients face an unprecedented decline in revenues as a result of the government ordered shutdown. Utilities are not facing the same level of revenue decline.

LPMA reiterates its position that the utilities industry in Ontario should be treated the same as any other industry, with the exception of the necessity to maintain financial viability. Allowing utilities that are making a profit and that are not experiencing any issues with their financial viability to recover costs associated with complying with government actions aimed at providing relief to ratepayers would be like the government imposing a service charge on all businesses that applied for the Canada Emergency Wage Subsidy program and on individuals that applied for the Canada Emergency Response Benefit.

LPMA's comments with respect to the recovery of lost distribution revenue from lost load are provided under Section 5.5.2 below.

<u>5.3.2 Additional Considerations for Customer-Driven Impacts</u>

The pandemic has not resulted in incremental bad debt or lost distribution revenues. It is the impact of the pandemic on the economy that has impacted not only utilities but virtually every other industry in the province.

LPMA does not believe the Board should view the pandemic as a once-in-a-lifetime event when it comes to viewing the impact on utilities. Rather, it should view the impact on the utilities of the current economic down turn as a regular recurring event.

As shown in Appendix B to these submissions, the utilities sector in Ontario has been subject to negative real GDP economic growth in 31 of the last 55 quarters from 2007 through to the third quarter of 2020.

As noted in Section 3 of these comments, based on the real GDP reduction of 1.9% in 2020 Q2, this decrease is only tied for the 12th worse in the last 55 quarters since the beginning of 2007. Three of these quarterly declines exceeded 5%.

Clearly, the utilities industry has endured frequent economic downturns that were driven by a myriad of causes. In addition to being frequent, these downturns have been more severe than the current decline for utilities and have been longer and deeper. The 2008-2009 recession saw 4 consecutive quarters of decline, totalling more than 6%. The decline in 2015 of 3 consecutive quarters totalled more than 11%.

LPMA also notes that in their December 15, 2020 COVID-19 Impact Study, LEI states that *"although utilities have seen negative revenue and cost pressures as a result of the pandemic, the observed financial impact has so far been controlled"* (page 1).

The need for special considerations for the customer-driven impacts on bad debt and lost revenues should be viewed in the light of the above. LPMA submits that there is no need, beyond the necessity of ensuring the financial viability of all utilities, as to why there should be any deviation from past Board practice with respect loss of revenue associated with load or increased bad debt. Both of these impacts are the realization of an aspect of the business risk that the approved ROE is designed to compensate for.

LPMA submits that in some respects the source of the net incremental costs is not important. It is clearly not important if the utility does not pass the means test. It is also not important if a utility passes the means test but is not in a position where its financial viability is threatened. When a utility does prove that its financial viability is in jeopardy, does it really matter if the costs they recover are the result of bad debt, lost revenues or other net costs? LPMA submits that it does not.

Consider a hypothetical example, where the amount in the Account is comprised of $40 in bad debt, $50 in lost revenue and $10 in other net costs for a total of $100. Further suppose that the utility has passed the means test and that if it recovers $40 of the amount in the Account, it will be able to maintain its financial viability. Does it really matter if the $50 it recovers is $40 for bad debt and $10 for other net costs or $50 for lost revenue,

or some other combination of all 3 of these costs? Clearly it does not. What does matter is the total dollars recovered.

In a similar example, consider a utility that passes the means test and the Board determines that it needs $120 to maintain its financial viability. Would it matter if the amount in the Account was $100 or $200? If the answer is yes and the amount in the Account is $100, and the amount eligible for recovery is capped at 100%, then the utility will not be able to maintain its financial viability. If the amount in the Account was $200 then it only needs 60% of the amount to do so. If the answer is no, the amount in the Account does not matter because the Board will allow the utility to recover $120 to maintain its financial viability, effectively eliminating the cap of 100% recovery of the amounts in the Account.

Specific comments related to revenue impacts are provided in Section 5.5.2 and in Section 5.5.4 for bad debt.

5.4 Application of Means Test for Recoverability

5.4.1 Basis for Means Test

LPMA supports the use of a means test to ensure that only utilities that are not able to maintain their financial viability qualify for any recovery of amounts in the Account.

LPMA does not, however, support the means test as proposed by Staff. Staff recommend that the means test be based solely on the ROE falling below the lower level of the dead band, that being 300 basis points below the Board approved ROE embedded in rates. LPMA submits that this means test is too simplistic.

While LPMA agrees with Staff's view that utilities operating within the dead band are effectively managing within a reasonable degree of earnings fluctuation and have maintained their opportunity for fair compensation and should be able to ensure the maintenance of their financial viability, LPMA does not agree that an ROE that falls below the dead band means that the financial viability of a utility is threatened.

In other words, falling below the 300 bps lower end of the dead band is a necessary condition to qualify for recovery of amounts in the Account, but it is not sufficient by itself.

LPMA submits that its position is supported by the findings of LEI in its *Report on the OEB's Cost of Capital Parameters and the Impacts of COVID-19* dated December 15,

2020. At page 10 of that report, LEI states that *"Utilities in Ontario appear to be fairly compensated for their risks based on current parameters."*

The LEI reports also states (at page 10) that *"Recognition of an allowed return on equity acknowledges that utilities are not risk free; utilities cannot expect to both earn an equity return and have the financial consequences of risk eliminated. Rate design already incorporates a number of shock absorbers for utilities, including a portion of rates which are not volumetric, treatment of bad debt expense (although recoverability is not assured), and some compensation for lost volumes associated with energy efficiency. Increases in residential load have in some cases offset declines in other customer loads. Furthermore, the overall drop in weather-normalized demand is far lower than the decline in business experienced by many industries, ranging from transportation to dining."*

With respect to the LEI statement that increases in residential load have in some cases offset declines in other customer loads, LPMA notes that most electricity distributors have already shifted to recovery of distribution costs based on a 100% fixed charge recovery and no volumetric based recovery. This shift was to protect utilities from risks associated with declining average use in this sector beyond lost revenue associated with energy conservation and from the risk associated with weather fluctuations. This has provided a significant reduction in risk to utilities since for many of them, the residential sector is the largest source of distribution revenue. In fact, based on the 2019 Yearbook of Electricity Distributors for the total industry, distribution revenues from the residential sector accounted for more than 60% of total distribution revenues. This reduction in risk to the utilities has not been accompanied to date by a reduction in the risk premium. It is somewhat ironic that the move to 100% fixed charge recovery for the residential sector has effectively deprived the utilities of additional distribution revenue from this sector that would help offset declines in the other sectors.

The LEI report noted above concludes that *"there is little evidence to date that utilities have suffered consequences of COVID-19 for which they are not already being compensated"* and that *"provided utilities are allowed a reasonable opportunity to recover their costs from ratepayers (including carrying costs), specific risks to the utilities sector should not impact their cost of capital."*

LPMA submits that a properly designed means test will provide utilities that are not able to maintain their financial viability with a reasonable opportunity to recover a sufficient portion of their costs from ratepayers to remain financially viable. Those utilities that do not pass the means test do not need to recovery any costs since their financial viability is not in question due to COVID-19.

In the following section, LPMA sets out what is believes is a reasonable means test to ensure that ratepayers shoulder the burden of COVID-19 net incremental costs only to the extent necessary to ensure that their utility remains financially viable.

5.4.2 Earnings-based Means Test

LPMA submits that the means test proposed by Staff should be considered as only a starting point for a proper means test to ensure that only utilities that require assistance from their ratepayers to maintain their financial viability should qualify to recover any amounts from their customers.

With respect to the use of a +/- 300 bps from the Board approved ROE embedded in rates, LPMA has a concern with the use of this dead band, which comes from the off-ramps established by the Board, if other components of the means test are not changed from that proposed by Staff.

As indicated in the *Filing Requirements for Electricity Distribution Rate Applications – 2020 Edition for 2021 Rate Applications – Chapter 3 Incentive Rate-Setting Applications* dated May 14, 2020, Section 3.3.5 states that:

> *"For each of the OEB's three rate-setting options, a regulatory review* ***may be triggered*** *if a distributor's earnings are outside of a dead band of +/- 300 basis points from the OEB approved return on equity. The OEB monitors results filed by distributors as part of their reporting and record-keeping requirements and determines if a regulatory review is warranted. Any such review will be prospective, and could result in modifications, termination or the continuation of the respective Price Cap IR or Annual IR Index plan for that distributor."* (emphasis added)

The key phrase here, in the view of LPMA, is that a regulatory review MAY be triggered if a distributor's earnings are outside of the dead band. The filing requirements do not say that a review WILL be triggered. Staff has indicated that in its view, this dead band of +/- 300 bps around the approved ROE is a range of fluctuations that can be reasonably expected year over year (Staff Proposal, page 13). LPMA strongly disagrees.

LPMA is aware that many utilities have fallen below the lower end of this dead band over the last several years and no regulatory review was triggered. In determining not to initiate a regulatory review, the Board was implicitly indicating that falling below the lower end of the dead band in any given year did not impact the financial viability of the utility. In fact, there have been several utilities that have fallen short of the lower end of

the dead band in 2 or 3 years over the last few years. As far as LPMA knows, none of these utilities have approached the Board with concerns about their financial viability.

In short, and as noted above in Section 5.4.1, falling below the lower end of the 300 bps dead band is a necessary but not sufficient condition to qualify for assistance from ratepayers.

LPMA provides comments on what it calls a multi-pronged approach to setting an appropriate and effective means test that provides ratepayer assistance to those utilities that require it to maintain their financial viability while at the same time ensuring that ratepayers do not bare any unnecessary costs that would enrich shareholders.

<u>300 bps Dead Band</u>

As noted above, LPMA submits that falling below the bottom level of the 300 bps dead band is a necessary but not sufficient criterion for meeting the means test. For example if the lower end of the dead band for a utility is 6.0%, there is no evidence that the financial viability of the utility is threatened at 5.99%, but maintained at 6.0%.

LPMA submits that the 300 bps may be too small. However, given that this is the magnitude associated with off-ramps, LPMA accepts the use of the 300 bps shortfall in the ROE as an appropriate first hurdle for a utility to pass in a multi-pronged means test in order to qualify for assistance. The utility will also be required to pass other components of the means test.

<u>Starting Point for the Dead Band</u>

Staff have proposed that the dead band be around the Board approved ROE embedded in rates. LPMA believes that there are more appropriate starting points that are more fair to both utilities and ratepayers. LPMA provides two distinct options.

<u>Option 1 – Lowest Board Approved ROE Embedded in Rates in 2015-2019</u>

Under the current Staff proposal, a utility would qualify if its ROE was 300 bps below the ROE embedded in rates. The ROE embedded in rates for 2015 rates was 9.30%, for 2016 was 9.19%, for 2017 was 8.78%, for 2018 was 9.00% and for 2019 was 8.98%. This means that under the Staff proposal there would be different ROEs that would pass the means test. For example, a utility that rebased in 2016 would have a 6.19% threshold to pass, while a utility that rebased in 2017 would have a 5.78% threshold. This does not appear equitable to LPMA to either utilities or their ratepayers. It also highlights the lack of sufficiency criterion noted above. Under the Staff proposal the utility that rebased in

2016 would be considered to have its financial integrity impaired if it earned less than 6.19%, while the utility that rebased in 2017 would have its financial integrity impaired if it earned less than 5.78%. If the 2017 rebaser earned between 5.78% and 6.19% it would not qualify for relief, while the 2016 rebaser would.

If the lowest Board approved ROE for the 2015 through 2019 period was used (i.e. 8.78%), then all utilities would be treated on an equitable basis. It does not make sense to have different ROE eligibility requirements based on when a utility rebased. If a utility is considered financially viable at 5.78% because it rebased in 2017, a utility that has a higher embedded ROE should also be considered to be financially viable at 5.78%. Financial viability is determined by actual earnings, not the forecasted amount built into rates.

This approach is also the most equitable for ratepayers. Staff's proposal includes limiting recovery up to the lower end of the dead band, which LPMA supports. However, the lower end of the dead band is different based on when the utility rebased, then ratepayers will end up paying more to those utilities that rebased in the higher ROE years. And again, if a 5.78% ROE is adequate for some utilities to maintain financial integrity, why is it not adequate for all utilities regardless of when they rebased? Ratepayers should only be required to provide assistance up to the level required to maintain financial viability, which based on the Staff approach, as modified, is 5.78%.

Option 2 – Lower of ROE Embedded in Base Rates & Average Actual ROE in 2015-2019

A second approach to determining an appropriate ROE to which the 300 bps dead band would apply would be to set it the lower of the ROE embedded in base rates and the average actual ROE over the 2015 to 2019 period for the utility. This approach mimics the approach set out in Section 5.2 of the Staff Proposal for measuring incremental impacts where Staff propose that when measuring discretely identifiable incremental savings to be recorded in the Account the baseline to be used would be the lower of the amount embedded in base rates and the lowest actual annual amount over the past five years (2015 to 2019).

Rather than the lowest ROE over the 2015 to 2019, LPMA believes that the average ROE over this period would be more appropriate. Financial viability is not determined on the basis of one year of earnings or losses. Rather, it is a longer-term concept, and as such, the profitability of a company over a longer period than one year is more closely related to financial viability.

The justification for this approach is that if a utility has under earned, on average over the last five years, then at least part of the under earning in 2020 is likely attributable to the same reasons that it under earned over the last five years. This portion of the under earning which is not related to COVID-19 should be removed for the means test, otherwise the utility could pass the 300 bps portion of the means test for reasons that are not COVID related and are simply a continuation of the past under earning.

There may be some instances where a utility has suffered significant losses over the past five years and have a negative ROE. In such circumstances, LPMA would suggest the removal of a clearly abnormal year or years from the calculation of the average ROE.

Was the Utility Financially Viable Before COVID-19?

LPMA has noted elsewhere in these comments that several utilities have under earned by more than 300 bps over the past several years. Some of the under earnings were significant. LPMA submits that the Board should deal with these utilities on a case-by-case basis to determine if they were financially viable or financially impaired before the onset of COVID. In such cases, the Board should ensure that ratepayers do not provide assistance to their utility for past issues. The financial viability of a utility should not be enhanced over its level at the end of 2019 in these circumstances.

The following comments are related to the need for a multi-pronged means test. In order for a utility to qualify for ratepayer assistance, LPMA believes that the utility should pass each of the following tests as well. This is not proposed to be an exhaustive list but an indication of some of the high-level components that should be included in a means test.

The list that follows is based on the need for the utility to demonstrate that it has acted prudently and done everything in its power to minimize the impacts of COVID and has fully exploited all available cost-reductions and savings.

Suspension of Dividends

LPMA submits that any utility that has paid dividends to its shareholder in 2020 should be deemed ineligible for the recovery of any amounts in the Account, regardless of whether or not they have an ROE that is below the lower end of the dead band. If the financial viability of a utility is being questioned, it should not be paying dividends to its shareholders. That money should be kept in the utility to assist in cash flow and to strengthen its balance sheet in order to maintain financial viability. Doing otherwise would be imprudent.

Ratepayers should not be expected to provide assistance to the utility if the utility does not take all steps to maintain its own financial viability, including the suspension of dividends.

If the Board were to allow a utility to require assistance from its ratepayers while at the same time allowing the payment of dividends to the shareholders, LPMA would expect the Board to lose credibility with the ratepayers that it is supposed to protect with respect to prices. We have already seen a similar backlash by taxpayers towards the government and towards companies that have received government assistance while at the same time making dividend payments to shareholders.

Payment of Employee Bonuses

LPMA submits that any utility that paid bonuses to its employees in 2020 should be deemed ineligible for the recovery of any amounts in the Account, regardless of whether or not they have an ROE that is below the lower end of the dead band. If the financial viability of a utility is being questioned, it should not be paying bonuses to its employees. That money should be kept in the utility to assist in cash flow and to strengthen its balance sheet in order to maintain financial viability. The payment of any such bonuses should, at a minimum, be deferred until the utility is on sound financial grounds. Doing otherwise would be imprudent.

Ratepayers should not be expected to provide assistance to the utility if the utility does not take all steps to maintain its own financial viability, including the suspension or deferral of employee bonuses.

If the Board were to allow a utility to require assistance from its ratepayers while at the same time allowing the payment of bonuses to employees, including the utility executives, LPMA would expect the Board to lose credibility with the ratepayers that it is supposed to protect with respect to prices. We have already seen a similar backlash by taxpayers towards the government and towards companies that have received government assistance while at the same time making bonus payments to employees.

If any bonus payments are made because of contractual requirements between the utility and its employees, then LPMA submits that the cost of the bonus payments should be recorded as a credit to the amounts in the Account. Ratepayers should not pay for employee bonuses if the financial viability of the utility is in question.

Request for Government Assistance

There are a number of government programs available to assist businesses from the federal and provincial governments. Utilities will be eligible for some but not for others. For example, smaller utilities with less than 100 employees may be eligible for the Ontario COVID-19 Business Support Grant, but not be eligible for the Canada Emergency Wage Subsidy program because the decline in their revenues did not exceed the threshold set by the federal government.

LPMA submits that the utilities should be required to file evidence if they apply for any assistance from ratepayers that have applied for every government program that is available and if they did not, indicate why they did not meet the eligibility requirements for those programs.

Any assistance received by the utility should be reflected as a credit in the Account. In addition any assistance that could have been received but was not because the utility did not apply should be recorded as a credit to the Account. This approach would ensure that the utility acted prudently in accessing government assistance or that it should have.

Debt Refinancing

One of the impacts of COVID on the economy is a reduction in interest rates. LPMA submits that a prudent utility should have taken whatever steps it could to replace existing debt instruments with lower cost debt. Such steps can have a significant impact on the financial viability of a company. Failure to do so would be imprudent on the part of the management of the utility.

The replacement of existing debt with lower interest rates may include breakage costs associated with the existing debt instrument. LPMA submits that the standard approach to dealing with these costs is to amortize them over the remaining life of the new debt instrument. If this amortized cost plus the interest cost on the new debt is less than the interest cost on the existing debt, costs to the utility can be reduced, enhancing its financial viability. Any such savings would be included as a credit in the Account.

If a utility fails to at least investigate this option to reduce costs, it should not be eligible for recovery of any amounts from ratepayers. Alternatively, the Board could impute the level of potential savings and add that figure as a credit to the amount in the Account.

Affiliate Debt

LPMA submits that affiliate debt is a special situation related to debt refinancing. In most cases the affiliate debt is with the shareholders of the utility or with an affiliate that is controlled by the shareholders. Some of this debt is at rates that considerably higher than the current market rates.

Like the suspension of dividends, LPMA submits that the shareholders of the utility should take steps to ensure the financial viability of the asset they own, similar to what any company in a competitive sector would do. These steps could include the deferral of interest payments to a future period, or the replacement of the affiliate debt with either affiliate or non-affiliate debt based on current market rates.
Again, failure of the utility owners and management to explore and do everything possible in order to ensure the financial viability of their own company would not be prudent and the results should not be visited upon the shoulders of ratepayers.

Staff Reductions/Vacancies/Other Costs

LPMA submits that ratepayers should not be expected to provide assistance to the utility if the utility does not take all steps to maintain its own financial viability, including reducing the level of staffing on a temporary or permanent basis, including not replacing employees that may have left before or during the pandemic. For a utility that is facing financial viability issues, not doing this would be imprudent. Utilities should be expected to show and explain what steps it took with respect to staff reductions and vacancies in order to maintain its financial viability.

Similarly, utilities should be able to show that they tried to reduce other costs as much as possible. These other costs could be consulting costs, repair & maintenance costs, tree trimming costs, etc. Such actions would include the deferral of OM&A spending to a future year.

Emergency Preparedness Plan & Execution

LPMA agrees with the Staff Proposal (page 15) that the extend to which a utility had emergency preparedness plans to deal with a wide range of emergencies can and should be used as one criterion in assessing prudence. LPMA supports the Staff proposal that the demonstration of well-executed disaster recovery plans, appropriate planning processes, and pivots in business plans appropriately carried out is a key aspect of demonstrating prudence.

Should Recoveries be Limited?

LPMA agrees that recoveries for any utility that passes the various components of the means test should be limited so that the lower end of the 300 bps threshold is not exceeded as a result of any amounts it recovers. This would eliminate the potential that utilities that under earn and pass the thresholds for recovery could end up in a better financial position than a utility that was operating within the dead band. This does not, however, mean that a utility should automatically recover and amount that brings the ROE up to the lower end of the dead band.

LPMA does not agree that the lower end of the of the typical 300 bps dead band is appropriate for the purposes of cost recovery eligibility. As noted above, LPMA has proposed other components of a multi-pronged means test.
LPMA also does not agree that for utilities that pass all components of the means test that financial viability means having their earnings raised to the lower bound. A utility can be financially viable with an ROE in 2020 less than 300 bps below the ROE embedded in their rates. This has been demonstrated time and time again, with numerous utilities falling below the dead band and not requiring assistance from its ratepayers. Clearly these utilities have remained financially viable or the Board would have stepped in to make sure that was the case.

5.5 Specific Sub-Accounts

5.5.1 Overview of the Sub-Accounts

As noted under the submissions in Section 5.3.1 above, LPMA does not agree with Staff that there should be a separate treatment for the costs necessary to comply with government or Board actions aimed at providing rate relief to ratepayers in response to the pandemic. However, should the Board adopt that proposal, then LPMA believes that a discrete sub-account should be established for each of the items noted below:

- Implementation cost of emergency time-of-use rates and deferred global adjustment charges for electricity distributors
- Implementation and administration costs of CEAP and CEAP-SB
- Increased LEAP EFA funding
- Lost revenues from certain reduced/waived specific service charges and
- Incremental bad debt directly attributable to the extension of the winter disconnection ban.

LPMA believes that these discrete items should be tracked separately so they can be tested for reasonability, to ensure that only the amounts associated with costs necessary

to comply with government and Board actions are included, and to be able to benchmark against other utilities.

5.5.2 Revenue Impacts

LPMA does not agree with the Staff Proposal that gains and differences in load and production should be eligible for recovery provided that they are incremental and attributable to the pandemic. This would be a significant deviation from the approach taken historically by the Board. The Board has in the past disallowed Z-factor treatment related to lost revenue associated with a significant reduction in electricity consumption and stated that *"the Z-factor criteria were not intended to be used for the recovery of revenue losses"* (EB-2009-0332, Horizon Utilities Corporation, Decision dated March 24, 2010, page 10).

In the EB-2004-0527 Amended Reasons for Decision dated May 11, 2005 for Oakville Hydro Electricity Distribution Inc., at page 3 the Board stated that *"The rates authorized by the Board and charged by the utility are expected to allow the utility to recover the costs it incurs to provide distribution service. Rates are set at a level that provides the utility an opportunity to earn a return on equity to compensate it for the risks it incurs; they are not set to guarantee the recovery of the allowed return."*

LPMA submits that there is no reason to abandon this non-qualification of lost revenues for recovery. It did not and does not qualify for Z-factor treatment and it should not qualify for any type of recovery, except as part of the Account for a utility that has proven it is not financially viable without recovery of at least some part of the Account.

Regulation is needed to serve as a proxy for competition. As is stated in the Staff Proposal (page 4), in the competitive environment, many businesses have incurred, and continue to incur, losses attributable to the pandemic. In a competitive environment, these businesses will not be able to charge customers for past lost revenues. Many of these customers will have simply disappeared because they have gone out of business. These remaining businesses cannot simply increase their prices in order to recover their lost sales revenues from their remaining customers. These customers would likely migrate to a business that was not trying to recoup its lost revenues through higher prices.

LPMA submits that a recovery mechanism that insulates utilities to any degree from the negative economic impacts of the pandemic would be badly misaligned with the Board's role to mimic competitive forces. Again, the only distinction that should be applied is the necessity of maintaining financial viability of an essential service provider.

With respect to any circumstances where lost distribution revenue is deemed to be recoverable through the Account, LPMA submits that the LEI approach to estimating the lost revenues is a step in the right direction.

The growth factor “g” should be calculated for each rate class and for each billing determinant within the rate class. This means that for any residential rate classes in utilities that have moved to a 100% fixed cost recovery, there is no need to calculate a “g” factor for the kWh’s for that class, but for a utility that has not yet moved to a full 100% fixed charge recovery, it would be required.

Since the “g” factor should not include any impact of weather, it should be calculated based on the annualized percent change between normalized actual billing determinants for 2019 and normalized actual billing determinants for the last approved test year.

The Board approved forecast should not be the starting point for the calculation of the growth factors in the billing determinants because this would not constitute an apples-to-apples comparison in that the growth should be based on actual to actual, not forecast to actual.

The Board may need to determine on case-by-case basis the normalization methodology that is to be applied to both 2019 and the base test year. The methodology should be based on the normal forecasting methodology used by the utility in the test year. However, there may be instances where the methodology used is not appropriate or adequate for the purposes of determining load variations.

Once the growth factors for all of the billing determinants for all of the rate classes have been calculated based on a normalized actual to normalized actual basis, these factors should then be applied to the normalized 2019 billing determinants to arrive at an estimate of the 2020 billing determinants. These estimates would then be compared to the normalized actual 2020 results, where the normalization methodology would be the same as for 2019 and the test year. In all cases, the normalization should be based on the heating and cooling degree days utilized in the Board approved forecast for the test year.

The difference for each billing determinant in each rate class between the estimated 2020 figures and the normalized actual figures would then be calculated.

Up to this point, the difference can be said to be attributable to the impacts of the pandemic and other factors, since the impact of weather has been removed. Before applying the rates for each of the billing determinants in each of the classes to calculate the distribution revenue difference, LPMA submits that another adjustment needs to

made to account for other factors other than the pandemic that may have impacted the 2020 load.

While the calculation of a standard deviation for each of the billing determinants in each rate class would be the most accurate approach to estimating the non-weather non-pandemic impacts on changes in the billing determinants, this would require the normalization of these billing determinants for several more years than just 2019 and the test year. A simpler approach would be to assume that 50% of the difference is due to the pandemic and 50% is due to other factors (such as CDM, normal efficiency gains as appliances are replaced, etc.).

5.5.3 Other Costs and Savings (including Financing Amounts)

LPMA supports the use of this account to catch all other costs and savings that are not captured elsewhere in the Account.

LPMA agrees with Staff that interest expense related to incremental borrowing costs beyond baseline levels should be eligible for recovery. However, LPMA notes that the opposite may also be true for some utilities. That is, their borrowing costs could be lower than baseline levels. The reasons for this are two-fold. First, interest rates may be lower than those built into the baseline, and second, there may have been a reduction in the baseline working capital allowance requirement as the result of a reduction in the cost of power due to load loss. The onus should be on the utility to provide a direct link between the difference in the interest expense related to incremental/decremental borrowing costs from the baseline level.

LPMA also agrees with Staff that the benefits of lower interest rates, which are a direct result of the impact of the pandemic on the economy, payment deferrals, or any other gains (and costs) to be made from strategic refinancing in the current low interest landscape should also be recorded in the Account.

It is LPMA's expectation that utilities should be expected to minimize its financing costs and maximize these savings in order to protect its financial viability. This includes re-financing affiliate debt where the debt can be re-financed at a lower rate.

There may be costs/penalties associated with replacing existing debt instruments with lower cost debt. Any such breakage fees/costs/penalties should be amortized over the life of the new debt that replaces the old debt. If the difference between the new interest costs and the old interest cost plus the amortization of the breakage costs results in a lower net interest cost, then this saving should be included in the Other Costs sub-account. However, if the net interest cost is higher, this amount should not be included in

the sub-account because any decision to proceed with this re-financing would not be in the best interest of the financial viability of the utility.

5.5.4 Bad Debt

A large portion of the bad debt incurred by distributors includes the cost of the flow-through commodity costs that the distributors pass on to their customers without any markup.

In prior decisions (RP-2005-0020/EB-2005-0391, Milton Hydro Distribution Incorporated, Decision and Order dated April 12, 2006, page 7; EB-2007-0081, Chatham-Kent Hydro Inc., Decision dated March 17, 2008, page 5), the Board has stated that even though there is no explicit risk premium associated with the commodity element of bad debt, the overall premium is sufficient to provide adequate compensation to the utility's shareholders.

In the EB-2007-0081 Decision noted above, the Board also confirmed that bad debt did not qualify for Z-factor treatment. LPMA submits that there is no reason to abandon this non-qualification of bad debt for recovery. It did not and does not qualify for Z-factor treatment and it should not qualify for any type of recovery, except as part of the Account for a utility that has proven it is not financially viable without recovery of at least some part of the Account.

Regulation is needed to serve as a proxy for competition. As is stated in the Staff Proposal (page 4), in the competitive environment, many businesses have incurred, and continue to incur, losses attributable to the pandemic. In a competitive environment, these businesses will not be able to recover bad debt from their customers, many of whom will have simply disappeared because they have themselves gone out of business. They cannot simply increase their prices in order to recover their bad debt costs from their remaining customers. These customers would likely migrate to a business that was not trying to recoup its losses through higher prices.

LPMA submits that a recovery mechanism that insulates utilities to any degree from the negative economic impacts of the pandemic would be badly misaligned with the Board's role to mimic competitive forces. Again, the only distinction that should be applied is the necessity of maintaining financial viability of an essential service provider.

5.5.5 Potential Need for a Capital-Related Sub-account

LPMA submits that the Board should establish a capital-related sub-account as there is a potential need to include costs related to incremental capital spending, such as laptops

and IT infrastructure used to assist employees in working from home, as an example. This type of capital expenditures would not likely occur in the absence of the pandemic. The revenue requirement associated with the capital expenditures (including return on cost of capital, depreciation and income taxes) would be subject to inclusion in the amount in the Account.

If the Board allows the recovery of lost revenues from load declines, then, as submitted elsewhere, the reduction in the working capital allowance component of rate base should also be tracked and used as an offset to the lost revenue. In this case the capital-related sub-account would track the reduction in the working capital allowance that results from the reduction in power purchased and the reduction in the revenue requirement (cost of capital only) would be included in the Account.

Staff proposes that temporal shifts in the timing and execution of existing or planned capital projects would not be eligible for inclusion in the capital-related sub-account. LPMA believes that this would be appropriate for two reasons. First, the reduction in capital expenditures will be reflected in lower in-service additions to rate base which will increase the actual return on equity for the utility. Second, the need for new capital will be reduced reducing the pressure on the utility to borrow. In both instances, the financial viability of the utility will be enhanced.

LPMA submits that the Board should also take into consideration the impacts on ICM/ACM approved projects. While timing differences will be accounted for in variance accounts around the projects, the cancellation or indefinite deferral of a project for which amounts are being recovered in revenues, should be reviewed immediately and the rate riders suspended pending the Board receiving more information as to the need and new timing for the project. For projects that are suspended indefinitely, the Board should consider refunding any ICM/ACM revenues as soon as possible to ratepayers.

5.6 Other Considerations

5.6.1 Period of the Account

Staff recommends that amounts should be recorded in the Account until the utility's subsequent rebasing application, assuming that the utility is able to support costs in future years (i.e. post-2020) as directly attributable to the pandemic.

At the time of rebasing utilities would have an opportunity to reflect their new operating "normal" by incorporating the effects of the pandemic, if they are expected to persist in the test year and beyond, into their forecasts.

LPMA submits that while this approach may be appropriate for some utilities, especially those that are scheduled to rebase in a year or two, it may not be appropriate for other utilities. For example, a utility may not be scheduled to rebase for 4 years. If the amount in the Account is significant, the Board should consider requiring the utility to rebase earlier than scheduled in order to minimize the amount in the Account.

Of more concern to LPMA, however, are utilities that may propose to delay their rebasing applications. This could extend the time horizon that amounts are added to the Account. LPMA submits that the Board should either not allow utilities to defer their rebasing applications if they are or plan to recover amounts in the Account, or end the addition of amounts to the Account as of the beginning of the test year that was originally scheduled for rebasing.

5.6.2 Offsets – Cost Reductions from Government Assistance

In order to prove that recovery of amounts in the Account are required to maintain financial viability, a utility should be required to provide evidence that it has reviewed the eligibility requirements for all government related COVID programs that were in place for any part of 2020.

Further, if a utility applied for any program and was rejected, that information should be provided in the filing. If a utility did qualify for any assistance, the amount and timing of the amount(s) should be recorded and reflected in the Account. Any amounts of the funds, grants or government assistance that are not repayable should be credited to the Account.

Any repayable assistance should be described and tracked separately so that any savings associated with this assistance (such as finance cost savings) can be calculated and credited to the Account.

5.6.3 Carrying Charges

LPMA agrees with the Staff Proposal that carrying charges should apply to the Account and that the carrying charge rate applicable should continue to be derived using the existing prescribed interest rate methodology.

Staff state that the prescribed interest rate methodology is reasonable for the period during which the pandemic persists and that it sees no substantive reason to question the validity of the methodology at this time. LPMA agrees.

6. DISPOSITION MATTERS

6.1 General Disposition Considerations

6.1.1. Timing and Process for Disposition Requests

Staff submits that the Account should be treated as a Group 2 account, but unlike most Group 2 accounts, an application for disposition can be made outside of a rebasing application.

LPMA agrees with Staff that it would be preferable to dispose of this account, which requires a prudence review, as part of a rebasing application. This is because there is likely to be a strong link between the costs and lost revenues (if applicable) included in the Account and the forecasts of costs and revenues going forward as part of a rebasing application. It would be more efficient from a regulatory and prudence point of view if these were part of the same application.

However, LPMA notes that if the Account is solely related to the maintenance of financial viability, then it may be appropriate for the utility to file a separate stand-alone application for recovery of the Account if delaying the disposition to a rebasing application can be shown to have a negative impact on the financial viability of the utility in the interim.

LPMA further submits that the OEB should take into consideration the position of a utility within IRM time horizon. For example, for a utility for which 2020 was the first year of IRM, and for which its financial viability is threatened, it should not wait until the next rebasing to dispose of the account. In this case, a separate stand-alone application may be warranted. At the other extreme, for a utility for which 2020 is the final year before its scheduled rebasing, then a separate stand-alone application may not be justified.

The OEB should also take into consideration of the magnitude of the amount to be recovered through the Account. The financial viability of a utility may not deteriorate if the amount to be recovered from the Account is relatively small, while the financial viability of the utility could be subject to further deterioration if the amount to be recovered from the Account is relatively large.

LPMA submits that the Board should consider the request for disposition outside of a rebasing application on a case-by-case basis taking into consideration both the amount in the Account and the timing of the next rebasing application for the utility.

LPMA agrees with Staff that the earliest opportunity for the Account balance to be brought forward for review and disposition is likely to be the summer of 2021, after the audited balances as at December 31, 2020 are publicly available.

6.1.2 Interim Disposition

LPMA agrees that interim disposition of a partial amount in the Account should be considered on a case-by-case basis where the utility is facing financial viability concerns. Any amount recovered should be clearly subject to a claw back provision. If after a full review, a utility does not pass the means test or it passes the means test, but the amount to be recovered through the Account has been reduced to less than the amount recovered on an interim basis, the Board needs to be able to return the money to the ratepayers.

The Board should consider a cap on the percentage of the balance in the Account that can be recovered through an interim disposition. Such a cap could vary on a case-by-case basis and balance the need for assistance in maintaining financial viability of the utility and ensuring that ratepayers do not pay more on an interim basis than they ultimately do on a final basis.

Finally, with respect to interim disposition, LPMA submits that any utility that is approved for interim disposition should file an application as soon as possible following the audit of the Account balance for final disposition. This would minimize the time that the interim disposition would be in place and reduce any amounts that would be clawed back and refunded to ratepayers, with the associated issues surrounding the time value of money and intergenerational transfers.

6.1.3 Audited Account Balance

Consistent with the Board's practice of using audited account balances for the disposition of other deferral and variance account balances, LPMA believes that the final disposition of any balance in the Account should be based on an audited Account balance.

Proposed interim dispositions allowed by the Board may not have an audited balance for the Account at the time of the application and approval. LPMA submits that these requests should reviewed on a case-by-case basis.

6.2 Cost Allocation and Rate Design of Recovery Mechanism

LPMA agrees with Staff that utilities should propose any disposition (including interim) based on accepted allocation methodologies, billing determinants and recovery periods).

Wherever possible, costs and lost revenues (if applicable) should be tracked on a rate class basis and, if applicable, on a rate zone basis.

The ultimate allocation of the Account balance, which could be on an aggregate basis or on a line-by-line basis, should be determined on a case-by-case basis by utility. There are likely to be significant differences in the makeup of costs incurred by utilities. These differences can be driven by the size of the utility, the makeup of customer types, and other factors. This could result in different cost causation from one utility to another and this difference should be recognized when allocating and recovering the costs from different types of ratepayers.

7. OTHER ISSUES

7.1 Customer Consultation

The Staff Proposal is silent on the issue of the need for customer consultation. LPMA believes that the Board should live up to its principle of being customer focused.

The Board should require any utility that proposed to recover any amount from the Account to consult with its customers. This consultation should be prescriptive in terms of what information the utility provides to customers in order to get their feedback and comments.

In particular, the information provided to customers should be the dollar increase in monthly bills and the time that these charges would be in place. It should also explain why some customers may end up paying more for the loss of revenues in rate classes other than their own (for example, if residential customers need to shoulder part of the loss of load from a large customer or increased bad debt from commercial customers).

The information provided should also include the return on equity in the absence of the recovery and with the recovery in both percentage terms and in dollar terms. Other financial information should include the total value of bonuses paid in 2020 and the amount of dividends paid to the shareholder.

LPMA submits that this information should be provided to customers in advance of any recovery application and the results of the consultation should be included in the evidence filed.

As evidenced by the reaction of the general public to politicians who vacationed outside of the country while recommending that people not travel for non-essential purposes and the reaction to finding out that profitable companies that continue to pay dividends to

their shareholders or paying bonuses to their employees while taking advantage of government supports such as wage subsidies, the Board needs to be cognizant of the potential backlash from ratepayers if utilities are allowed to enhance shareholder profits over and above what is required to maintain financial viability on the backs of ratepayers, many of which find themselves in circumstances far worse than the utilities.

The backlash could be swift and hurt not only the utility involved but also the regulator and the industry in general. This negative impact could last years.

7.2 Full Transparency for Ratepayers

As noted above, the public is not in the mood for anything but full transparency. If any amounts are approved for recovery, LPMA submits that the amount recovered from a customer each month should be shown on a separate line. On the first bill including this new line item, a full explanation of the charge should be provided.

7.3 Future Over Earnings

The worst thing that could happen to the utilities industry and to the Board, as its regulator, would be for a utility to recover amounts associated with the Account and then over earn in the years when it is recovering this amount. Consider the following example.

A utility has an approved ROE of 9% and its actual ROE for 2020 is 4%, so the utility files an application in the summer of 2021 to recover some amount to enable it to maintain its financial viability. The Board allows the utility to recover an amount because without this recovery, the financial viability of the utility is not guaranteed and the rate rider is implemented for the beginning of 2022.

In 2021, the utility earns an ROE in excess of the approved level of 9%. Under the current rules, if the ROE is below the higher end of the deadband of 300 bps above the approved ROE, there is no review of rates. If the ROE is above the 300 bps deadband the Board MAY initiate a review.

In such a situation, ratepayers would assume that any over earning above the approved ROE should be used to maintain the financial viability of the utility, **in place of recovering that amount of over earning from ratepayers in the following year**. Failure to do so would be a complete failure of the regulatory regime and a failure to realize that financial viability is a long term concept, not one based on the results of one year, in isolation from other years.

Similarly, if the utility does not over earn in 2021 in the above example, but does so in 2022, the question still arises as to why the ratepayers should be expected to pick up the costs when a utility under earns and get none of the benefits when it over earns.

LPMA suggests that the Board should reduce the deadband on over earnings to 0 basis points for any utility that is recovering amounts from the Account for the duration of that recovery. For example, if the utility has a two-year recovery period associated with the Account, then the utility should have its deadband on over earnings reduced to 0 basis points for those two years and it would revert to 300 basis points when the rate rider is removed.

Further, LPMA suggests that it would be appropriate for any amount earned in excess of the approved ROE would be used to offset the amounts recovered through the Account. It would not be just and reasonable to expect ratepayers to pay to maintain financial viability of a utility without the shareholder contributing to that effort with any excess earnings.

7.4 Process

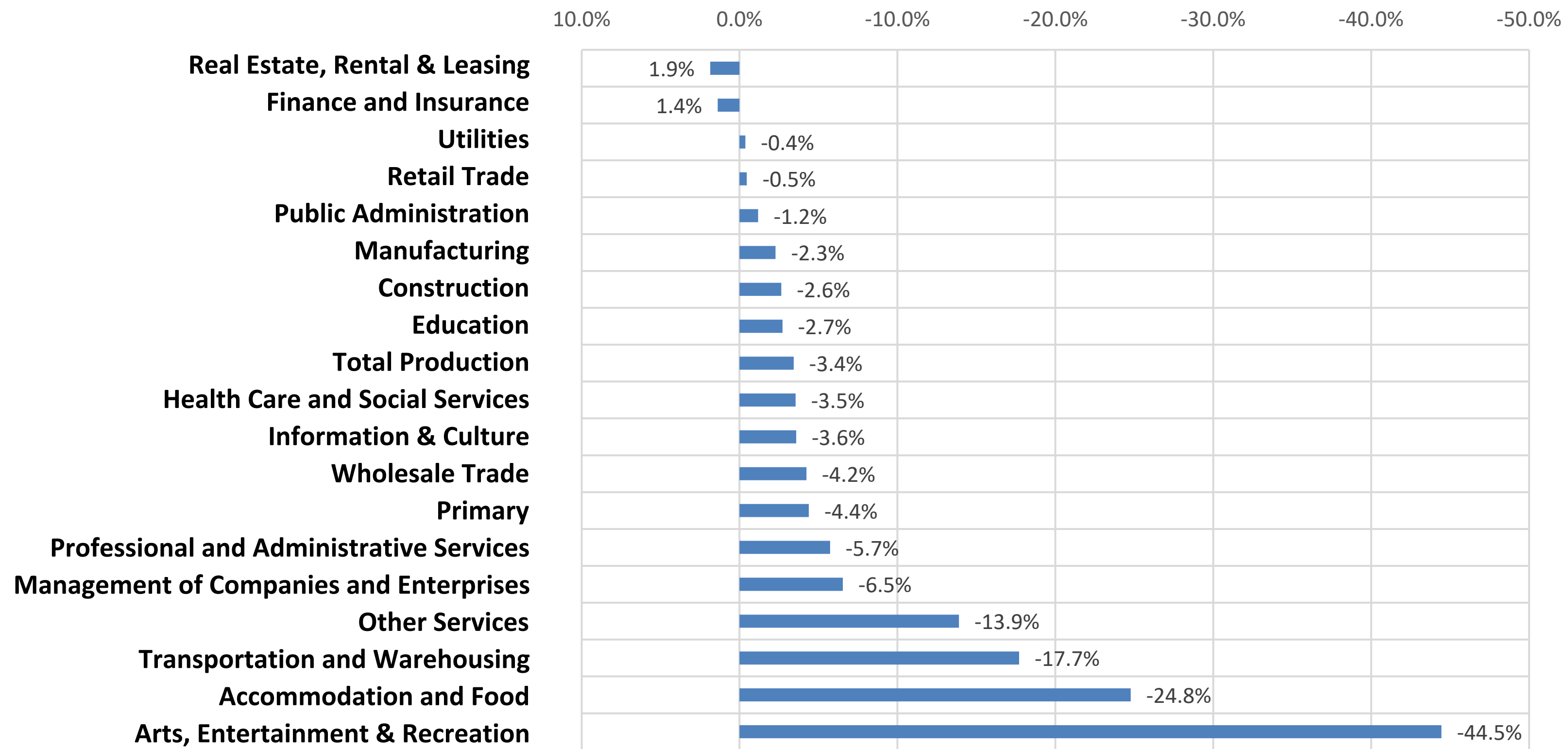
LPMA understands that Staff will review the stakeholder comments and the stakeholder reply comments of parties that are due on February 11, 2021 and then update their proposal into a more formal guidance. As indicated the in the Board's letter of December 16, 2020 re *Consultation on the Deferral Account – Amounts Arising from the COVID-19 Emergency*, the Board noted that it had not ruled out any opportunities for stakeholders to comment on a draft of the eventual guidance that will be issued.

Given the importance of this consultation and the potential magnitude of costs that could be allocated to ratepayers and importance of the financial viability of the utilities, LPMA strongly urges the Board to provide an opportunity for stakeholders to comment on a draft of the eventual guidance that will be issued.

Yours very truly,

Randy Aiken
Aiken & Associates

APPENDIX 1
REAL GDP CHANGE BY INDUSTRY 2020 Q1 TO 2020 Q3



Source: Ontario Ministry of Finance, Ontario Economic Accounts Tables, Table 15 - Ontario Production by Industry at 2007 Prices, seasonally adjusted data at annual rates, millions of chained (2012) dollars

APPENDIX 2