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BY EMAIL and RESS

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March 4, 2020
Our File: EB20200026

Attn: Christine Long, Registrar

Dear Ms. Long:

Re: EB-2020-0026 – Halton Hills Hydro Inc. – SEC Submissions on Unsettled Issue

We are counsel to the School Energy Coalition ("SEC"). Pursuant to Procedural Order No. 6, these are SEC's submissions on the unsettled partial issue (Issue 2.1) in Halton Hills Hydro Inc.'s ("HHHI") 2021 rates application regarding the appropriate calculation of the test year rate base related to its 2019 approved Incremental Capital Module ("ICM") for a new Transformation Station ("TS").

The Unsettled Issue

As set out succinctly in the Settlement Proposal, the parties are unable to agree on the following component of the rate base calculation, "Is HHHI's approach to applying the half-year rule (in the year the TS came into service) to the TS ICM costs included in the 2021 Test Year opening rate base correct or appropriate?"[1]. SEC submits that it has not.

The Board's adjudication of the issue is important, not just in the context of this proceeding, but more broadly, to provide guidance to distributors with respect to the proper treatment for the purpose of the rate base calculation of a previously approved ICM. There appears to be inconsistent treatment amongst distributors on this issue.[2]

In its application for 2019 rates, the Board approved HHHI's request for an ICM for the construction of a new TS that was scheduled to go into service in 2019. Consistent with the Board's Filing Requirements and various ICM policy reports, the ICM rate rider was calculated as if the TS was in-

[1] Settlement Proposal, p.18-19; SEC notes that the actual costs of the TS station where higher then was forecast and approved for the purposes of the ICM. This is not relevant for the purposes of the unsettled issue as part of the Settlement Proposal HHHI agreed to withdraw the request for a true-up of the variance in costs (Issue 5.3) and the parties accepted the final costs as reasonable to be collected on an forward looking basis as part of the 2021 rate base (settled component of Issue 2.1).
[2] For example, in Burlington Hydro Inc.'s 2021 rebasing application it recognized that it should have treated its 2019 ICM for the purpose of opening rate based on a similar full year basis. (EB-2020-0007, Interrogatory Response 2-Staff-33(a))

service for the entire 2019 rate year.[3] As the Board has noted in the past, as a general rate-setting matter, a half-year rule is applied in the first year that an asset enters service.[4] The Board takes a different approach in the context of calculating an ICM rate rider. With the exception of applications that are in the final year of an IRM plan, the Board does not apply the half-year rule as to not build in a revenue deficiency in subsequent years:

> The OEB's general guidance on the application of the half-year rule was originally provided in the Supplemental Report. In that report the OEB determined that the half-year rule should not apply so as not to build a deficiency for the subsequent years of the IRM plan term. This approach is unchanged in the new ACM/ICM policy. However, the OEB's approach in decisions has been to apply the half-year rule in cases in which the ICM request coincides with the final year of a distributor's IRM plan term.[5]

The question that arises is, for the purposes of determining the opening rate base in the first rebasing application after an ICM has been approved, is the Applicant required to treat the ICM as being in-service in the rate year the ICM was approved on a half-year basis (i.e. the general rate-setting method), or as if it was put in-service on a full-year basis (i.e. consistent with the approach in setting the ICM rate rider)? SEC submits that it is the latter approach that is correct and ensures there is no over-recovery from ratepayers as a result of a higher than appropriate test year rate base calculation and future depreciation expense.

Application to HHHI

Under the approach that is proposed by HHHI, it would over-collect from ratepayers because the ICM rate rider was calculated so that revenues were received based on the approved costs as if the TS was in-service for 2 full years. But for the purposes of opening rate base, HHHI would treat the TS as if it had been in-service for only 1.5 years. The impact in the test year is that the net book value ("NBV") related to the TS would remain higher since there would be less accumulated depreciation removed from the gross cost of the asset. This results in a higher rate base and a higher return on capital built into the 2021 revenue requirement.

SEC recognizes that the impact on the 2021 revenue requirement may not be material in HHHI's case because of the long depreciation life of a TS. But for other distributors the amount may be material depending on the type of asset that is at issue. Considering that often ICMs are for large technology projects such as CIS or GIS systems, which have very short depreciation lives, the difference would be very significant.

Where it becomes a material amount with respect to HHHI is the impact on the depreciation expense in the future. This is because with very limited exceptions, the additions to accumulated depreciation in a year must match the additions to the depreciation expense schedule. On that basis, HHHI has treated for the purposes of the depreciation schedule, as if the TS asset was brought in-service in 2019 under the half-year rule (treated as current year additions), as opposed to on a full-year basis

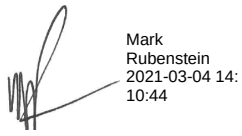
[3] *Decision and Order* (EB-2018-0328), April 4, 2019, p.4; Approved ICM Model included in the record in this proceeding, at Exhibit 2, Appendix 2-3
[4] EB-2014-0219, Report of the OEB on New Policy Options for the Funding of Capital Investments: Supplemental Report, issued January 22, 2016
[5] Filing Requirements For Electricity Distribution Rate Applications - 2020 Edition for 2021 Rate Applications, Chapter 3, Incentive Rate-Setting Applications, p.30

consistent with the amount of depreciation it received in 2019 in the ICM rate rider.[6] This means HHHI will ultimately recover an extra half-year's depreciation on the TS station (or more accurately the varying components of the TS station). The weighted average depreciation rate of the individual components of the TS station is approximately 44 years.[7] Under HHHI's proposal, customers will ultimately pay the same annual depreciation expense, not over 44 years but over 44.5 years, and thus overpay for the cost of the asset by 2.27%. This results in a material over collection by HHHI of $324,926.[8]

Summary

SEC submits to ensure ratepayers do not overpay for the TS station, the Board should reject HHHI's proposal, and require the inclusion of the TS station costs for the purpose of the opening rate base, and as a consequence the depreciation schedule, consistent with the full-year basis of the ICM calculation in 2019.

Yours very truly,
Shepherd Rubenstein P.C.



Mark Rubenstein

cc: Wayne McNally, SEC (by email)
Applicant and intervenors (by email)

[6] Appendix 2-C, Tab 2019 Dep Ex.; See aso Appendix 2-BA (2019 Year)
[7] See Appendix 2-C, Tab 2019 Dep Ex. Sum of total current year additions related to the TS (Account 1815) [g] divided by sum of Depreciation Expenses on Current Year Additions related to the TS (Account 1815) [n] x 2.
[8] This represents 1/2 of the annual depreciation based on the actual costs of the TS of $648,852 (See ICM Model with actual costs included at Exhibit 2, Appendix 2-3, p.1149