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March 4, 2021

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Our Matter Number: 1213607

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Ms. Christine Long
Registrar
Ontario Energy Board
27th Floor
2300 Yonge Street
Toronto, ON M4P 1E4

Dear Ms. Long:

Halton Hills Hydro Inc.
2021 Cost of Service Application
OEB File No. EB-2020-0026
Settlement Proposal – Unsettled Issue

Pursuant to Procedural Order No. 6, dated February 22, 2021, please find enclosed the submission for Halton Hills Hydro Inc. on the unsettled issue.

Yours very truly,

Richard J. King

RK:hi
Enclosure

c: All Parties to EB-2020-0026

EB-2020-0026

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, (Schedule B);

AND IN THE MATTER OF an application by Halton Hills Hydro Inc. for an order approving just and reasonable rates and other charges for electricity distribution beginning May 1, 2021.

HALTON HILLS HYDRO INC.

ARGUMENT

MARCH 4, 2021

Halton Hills Hydro Inc.
EB-2020-0026
Argument of Halton Hills Hydro Inc.

Filed with OEB: March 4, 2021

A. INTRODUCTION

Halton Hills Hydro Inc. (the "**Applicant**" or "**HHHI**") filed a Cost of Service application with the Ontario Energy Board (the "**OEB**" or the "**Board**") on August 27, 2020 under section 78 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, (Schedule B) (the "**Act**") seeking approval for changes to the rates that HHHI charges for electricity distribution and other charges, to be effective May 1, 2021 (OEB Docket Number EB-2020-0026) (the "**Application**").

On February 18, 2021, HHHI filed a Settlement Proposal with the OEB that resolved all but the following issue in the proceeding:

> **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?**

This unresolved issue fell within Issue 2.1 of the Issues List in the proceeding.

B. TREATMENT OF TS ICM COSTS (ISSUE 2.1)

2.1 Are all elements of the Revenue Requirement reasonable, and have they been appropriately determined in accordance with OEB policies and practices?

The Parties were able to reach agreement on all aspects of Issue 2.1 in the Settlement Proposal with the exception of the appropriate amount to be included in HHHI's 2021 opening rate base for HHHI's Municipal Transformer Station (the "**TS**"). The TS was the subject of an Incremental Capital Module ("**ICM**") application by HHHI (EB-2018-0328) (the "**TS ICM**"). In the TS ICM, the Board approved ICM funding of $23.48 million for HHHI's construction of a new TS. HHHI began recovery of these capital costs via rate riders approved by the Board effective May 1, 2019. The TS was permanently placed in service in November 2019.

In accordance with section 3.3.2.4 of the Filing Requirements for Electricity Distribution Rate Applications ("**Filing Requirements**"), dated May 14, 2020, the Board's half-year rule was not applied in 2019 in respect of the rate riders. However, for the purposes of calculating HHHI's opening rate base for the 2021 Test Year, HHHI employed the Board's normal practice of calculating the rate base value of the TS based on the half-year rule for 2019 and a full year of depreciation for the 2020 bridge year.

Intervenors are of the view that this is not appropriate, and that HHHI's opening rate base for the 2021 Test Year should reflect two full years of depreciation (2019 and 2020) to account for the non-application of the half-year rule to the rate rider by virtue of section 3.3.2.4 of the Filing Requirements.

Board Policy re: Half-Year Rule in ICM Applications

Section 3.3.2.4 of the Filing Requirements states:

> *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.* (emphasis added)

HHHI originally placed its TS in-service in May 2019. After a brief period of operation the need for additional commissioning activities, not anticipated in the initial commissioning plan, was identified and the TS was removed from service. Additional commissioning activities were conducted between May 2019 and November 2019, at which time the TS was returned to service permanently.

HHHI's last incentive rate-setting mechanism ("**IRM**") plan term was established by EB-2015-0074. The IRM plan term began on May 1, 2016 and it will end on April 30, 2021. Since the TS first entered into service approximately 12 months before the final year of HHHI's IRM plan term, HHHI did not apply the half-year rule,[1] as mandated by the OEB in section 3.3.2.4 of the Filing Requirements. The amount of depreciation calculated for 2019 was $608,789.[2]

The specific purpose of the exception is to ensure that the utility does not suffer a revenue deficiency in the interim period between cost-of-service proceedings, which would occur if it only recouped half its depreciation expense associated with the new asset during any IRM term. The exemption is meant to be operative solely in the IRM term.

The 2021 Cost-of-Service Application

As required by section 2.2.2.5 of the Filing Requirements, HHHI provided its capitalization policy in its Application in this proceeding (see section 2.3.8 of Exhibit 2). That policy describes HHHI's treatment of depreciation and amortization as follows:

> *Depreciation is recognized on a straight-line basis over the estimated useful life of each significant identifiable component of an item of property, plant, and equipment. Land and land rights are not depreciated. Assets under construction (work in progress) are not depreciated until the project is complete and in service.* ***Depreciation of an asset begins in the year when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended. For rate setting purposes, in the first year of service, depreciation is calculated using the ½ year rule.***

[1] Incremental Capital Module Rate Application, EB-20180328, Filed: December 3, 2018, p. 21.
[2] *Ibid,* Table 8 of TS ICM, at p. 20.

Depreciation of an asset ceases when the asset is retired from active use, sold or is fully depreciated. (emphasis added)

The useful life of the assets HHHI uses for depreciation purposes was derived from the HHHI Specific Kinectrics Report as filed in the 2012 Cost of Service. The componentization of HHHI assets for IFRS along with the useful lives was approved by the Board in HHHI's 2012 Cost of Service and was reproduce in HHHI's 2016 Cost of Service Rate Application. HHHI asset componentization and useful lives that was approved in 2012 and 2016 is reproduced in Exhibit 4.

This is in-line with long-standing Board practice. To comply with the capitalization policy, HHHI applied the half-year rule to determine the TS depreciation for 2019, which was the first year the TS was in service. In the 2020 bridge year HHHI applied a full year of depreciation to the TS. As a result, in the Application the TS was added to the rate base in the 2021 Test Year with one and a half years of accumulated depreciation.

By complying with the capitalization policy HHHI also maintained consistent fixed asset values for the TS components for both its regulatory reporting and financial reporting. Since HHHI's financial reporting required the application of the half-year rule in 2019, this consistent approach for both regulatory reporting and financial reporting avoided significant additional regulatory reporting efforts. Not applying the half-year rule for regulatory reporting purposes would have required HHHI to either manually record the fixed asset value for each component of the TS on a spreadsheet for the next 55 years (the longest useful life of a TS component) or establish a separate computerized accounting system for the sole purpose of recording TS fixed asset values for regulatory reporting. It is HHHI's position that the cost of such regulatory reporting efforts, combined with the potential risk of future reporting errors if a manual spreadsheet were used, are not warranted.

<u>Varying Treatment of the Half-Year Rule</u>

The appropriate treatment of ICM costs and opening rate base in subsequent cost-of-service applications has come before the Board before – with inconsistent outcomes. In EB-2012-0124, an ICM application by Festival Hydro Inc., the Board determined the half-year rule applied to the ICM costs of a new transformer station.[3] However, in Festival Hydro Inc.'s subsequent cost-of-service application the Board approved the inclusion of thirteen months of depreciation in the opening rate base.[4] Similarly, in EB-2010-0130 the Board determined the half-year rule did not apply to the ICM costs of a new transformer station built by Oakville Hydro Electricity Distribution Inc.[5] Yet, in the subsequent cost-of-service application the Board approved the application of the half-year rule in the opening rate base.[6] These two examples demonstrate that the half-year rule has been applied differently in an ICM application and a subsequent cost-of-service application.

[3] Decision and Order, EB-2012-0124, April 4, 2013, p. 9.
[4] Decision and Order, EB-2014-0073, April 30, 2015, p. 14.
[5] Decision and Order, EB-2010-0104, March 14, 2011, p. 18.
[6] Decision and Order, EB-2013-0159, April 17, 2014, Appendix C. See also Exhibit 2, EB-2013-0159, October 13, 2013, table 2-46.

C. CONCLUSION

HHHI's approach to this issue is reasonable. It followed: (a) its own capitalization policy (which reflects the Board's standard practice with respect to the half-year rule for deprecation of assets in their first year of service; and (b) the Board's policy with respect to an exemption from the half-year rule for the period leading up to next cost-of-service application. HHHI is not aware of any OEB guidance or requirements that contradict HHHI's approach. As a result, HHHI believes that its Application is in compliance with existing Board policy and HHHI's filed capitalization policy. Further, HHHI's approach will simplify and streamline the administration of HHHI's regulatory reporting of TS fixed asset values for the next 55 years.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 4th DAY OF MARCH, 2021

OSLER, HOSKIN & HARCOURT LLP
Per:

Richard King / ct

Richard J. King
Counsel to the Applicant

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