Shepherd
Rubenstein

**Mark Rubenstein**
mark@shepherdrubenstein.com
Dir. 647-483-0113

**BY EMAIL and RESS**

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
M4P 1E4

April 27, 2021
Our File: EB20200150

**Attn: Christine Long, Registrar**

Dear Ms. Long:

**Re: EB-2020-0150 – NextBridge 2022-2031 Rates – SEC Final Argument**

We are counsel to the School Energy Coalition ("SEC"). Pursuant to Procedural Order No. 5, please find a copy of SEC's Final Argument in the above-captioned matter.

Yours very truly,
**Shepherd Rubenstein P.C.**

Mark
Rubenstein
2021-04-27
11:10:06
Mark Rubenstein

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

**EB-2020-0150**

**ONTARIO ENERGY BOARD**

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

**AND IN THE MATTER OF** an Application by Upper Canada Transmission, Inc. operating as NextBridge Infrastructure, LP for an Order or Orders pursuant to section 78 of the Act approving rates and other charges for transmission of electricity.

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# FINAL ARGUMENT OF THE SCHOOL ENERGY COALITION

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**April 27, 2021**

**Shepherd Rubenstein P.C.**
2200 Yonge Street, Suite 1302
Toronto, Ontario M4S 2C6

**Mark Rubenstein**
Tel: 416-483-3300
Fax: 416-483-3305

**Counsel for the School Energy Coalition**

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# 1 OVERVIEW

***1.1.1*** Upper Canada Transmission Inc., in its capacity as the general partner, acting for and on behalf of the limited partnership, NextBridge Infrastructure LP ("NextBridge") filed an application with the Ontario Energy Board (the "Board" or "OEB") pursuant to section 78 of the *Ontario Energy Board Act, 1998*, for approval of its transmission revenue requirement for the period effective April 1, 2022, through to December 31, 2031 ("plan term"), based on a proposed Custom Incentive Rate-setting framework ("Custom IR").

***1.1.2*** NextBridge is a new utility which is completing construction of, and will operate, a single large transmission line in northwest Ontario that runs between Wawa and Thunder Bay (the "East-West Tie Line"). NextBridge was granted the leave to construct the East-West Tie Line in the Board's *Decision and Order* dated February 11, 2019[1], after the Lieutenant Governor-in-Council issued a directive on January 30, 2019, directing NextBridge's license to be amended, requiring it to be the entity to develop and seek approval to construct the line.[2]

***1.1.3*** This is the first application for a single asset transmission utility requiring full adjudication by the Board.[3] Unlike most other utilities who file rate applications with the Board, NextBridge's rate base, and its overall costs, decline over the length of its Custom IR term. Yet, NextBridge seeks approval of a Custom IR framework which increases its revenue requirement annually. As discussed in detail in this argument, this results in a proposed rate framework that ensures that NextBridge significantly over-earning. This is inappropriate and is neither just nor reasonable. The proposal requires significant modifications to ensure that there is a fair balance between the interests of customers and the company.

***1.1.4*** The Board regularly approves Custom IR frameworks that result in customers paying more than they would have under a price or revenue cap index, but only where it is warranted because

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[1] *Decision and Order* (EB-2017-0182/0194/365), February 11, 2019

[2] *Decision and Order* (EB-2017-0182/0194/365), February 11, 2019, p.5-6

[3] The Board has previously approved Settlement Proposals in proceedings involving applications by B2M LP (EB-2018-0275) and Niagara Reinforcement LP (EB-2019-0178). SEC was not an intervenor in either application. Neither proceeding had any significant ratepayer group involvement. The intervenors in the B2M LP proceeding were VECC and two labour unions (Society and PWU). There were no intervenors in the Niagara Reinforcement LP application. The Settlement Proposal was entered into between the company and Board Staff. We agree with NextBridge that those Settlement Proposals should not act as precedent for future cases (Argument-in-Chief, p.14).

the capital needs of a utility that cannot be recovered by an I-X adjustment.[4] It is only fair then that when the opposite occurs – the capital needs demonstrate that I-X would result in an over-recovery – that the Board use a symmetrical approach and reduce the annual adjustment.

***1.1.5*** This is the Final Argument of the School Energy Coalition ("SEC").

***1.1.6*** SEC has not addressed every issue in this application, but focused on the major components only. Silence on any given issue should not be construed as acceptance of NextBridge's proposal.

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[4] See for example, Hydro One Networks Inc. Transmission 2020-2022 (*Decision and Order* (EB-2019-0082), April 23 2020, p.22-23), Toronto-Hydro Electric System Limited 2020-2024 (*Decision and Order* (EB-2018-0165) December 19 2019, p.36, 40), Hydro One Networks Inc. Distribution 2018-2022 (*Decision and Order* (EB-2017-0049), March 7 2019, p.30-31)

# 2 RATE FRAMEWORK

## 2.1 *NextBridge Proposal*

***2.1.1*** NextBridge has proposed a Custom IR rate-setting framework that sets a 2022 annualized base year revenue requirement of $55.7M, determined on a cost of service basis, and then in each subsequent year of the plan term, inflates the previous year's approved amount through a Revenue Cap Index ("RCI").[5] The RCI formula is a traditional I-X approach, where the inflation factor is fixed at 2% and the productivity factor (including any stretch factor) is set at 0% for the entire term.[6] In short, the 2022 annualized base year revenue requirement increases each year by 2%, beginning in 2023 through to 2031.[7]

***2.1.2*** NextBridge's proposed 2% fixed inflation factor is based on the Board's 2020 inflation parameters.[8] It also proposes a 0% productivity factor including a 0% stretch factor. It does so not on the basis of any utility specific benchmarking study, but rather that it is "a new entrant and has structure unlike other transmission and distribution utilities in Ontario."[9]

***2.1.3*** SEC submits that even if one accepts that the proposed 2022 annualized base year revenue requirement of $55.7M is reasonable, the RCI approach to adjusting the annual revenue requirement is not.

***2.1.4*** NextBridge's revenue requirement is primarily driven by its initial capital costs.[10] Based on its proposed 2022 base revenue requirement, 91% of the $55.7M is made up of capital-related costs (return on equity, cost of debt, depreciation, and income taxes). [11]

***2.1.5*** Unlike almost every other utility that brings forward a rate application to the Board, NextBridge is not forecasting an increase in its rate base over its plan term. In fact, it is quite the opposite. NextBridge rate base will decline.

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[5] A-3-1, p.5-6, para.12 (K1.2, p.3)

[6] A-3-1, p.6, para.13-14 (K1.2, p.3)

[7] E-1-1, p.2, Table 3 (K1.2, p.6)

[8] Interrogatory Response OEB Staff #3(b)

[9] A-3-1, p.6, para.14 (K1.2, p.3)

[10] Tr.1, p.38

[11] Tr.1, p.38-39

*2.1.6* This makes sense. NextBridge is a single asset utility, where its opening 2022 rate base of $774.9M will include the entirety of the forecast construction costs of the transmission line ($737.1M), in addition to its phase shift costs ($5.33M), the upfront purchase of certain spares ($1.2M), and the previously approved development costs ($31.2M[12]). This consists of almost all of the capital expenditures that the utility will spend through to the end of its rate plan.

*2.1.7* As a new utility with a new asset, it expects to undertake little capital work after construction is complete. In addition to a small amount of $230K of additional in-service it plans to spend in 2022 (that is included in its 2022 rate base), between 2023 and 2031 it plans to spend a total of $4.05M in capital expenditures.[13] This is a fraction of its annual depreciation expense ($9.26M) and will result in reduction of the rate base annually over the plan term.[14] This is a fact that NextBridge does not dispute.[15] As a result of the declining rate base, its capital-related revenue requirement will also decrease over the plan term.

## 2.2 ***SEC Analysis***

*2.2.1* SEC undertook an analysis to calculate the gap between the revenue that would be collected under NextBridge's proposed rate-setting framework, and its forecast costs, including all planned capital expenditures through to the end of 2031. The analysis makes two assumptions. First, NextBridge's cost of capital parameters remain the same (as requested in the application) and are built into the 2022 annualized base year revenue requirement. Second, the OM&A costs increase annually at 2%, the same as NextBridge's proposed inflation factor.

*2.2.2* SEC referred to much of this analysis at the oral hearing.[16] At the hearing, NextBridge did not agree with some of the assumptions made, or the conclusion SEC was drawing from them, but did accept that the calculations (i.e. the math) were correct.[17] SEC has included copies in the

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[12] C-2-2, p.1; C-2-3, p.1; C-2-4, p.1; C-2-5, p.1 (K1.2, p.30-34); Tr.1, p.44-47

[13] Tr.1, p.48-49; B-1-7, Table 1(K1.2, p.46); Interrogatory Response OEB Staff #34(b) (K1.2, p.48)

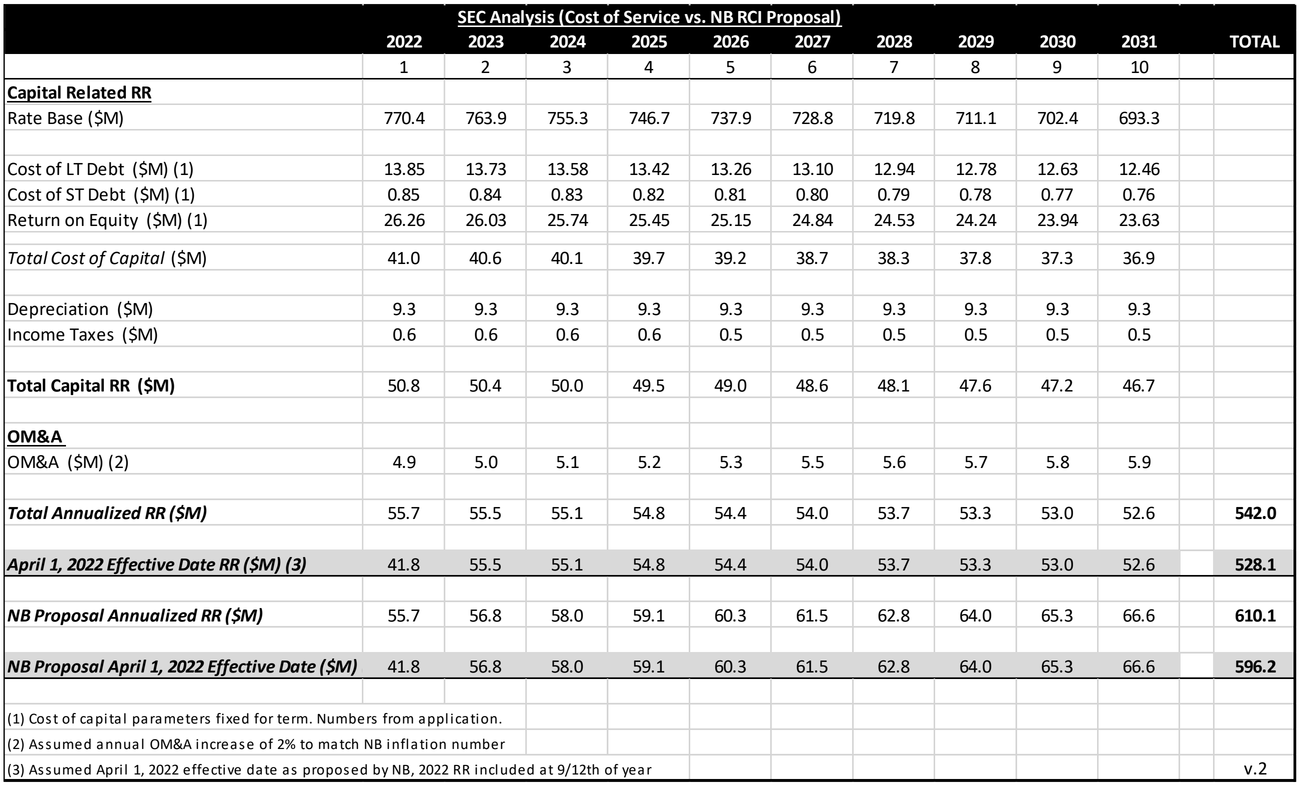
[14] F-11-1, p.1, Table 1 (K1.2, p.35)

[15] Tr.1, p.51

[16] These were the tables included in K1.2, p.56-57.

[17] In advance of the oral haring, SEC provided the spreadsheet to NextBridge and asked it to confirm the calculations/math. It returned a revised version that included a small error (see K1.2, p.57, Line 9) which SEC corrected in the version of the spreadsheets included in K1.2, p.56-57. See also, Tr.72-73; At the hearing, NextBridge made comment that it needed to review the tax calculations (Tr.1, p.137) although provided no reasons for why it was inaccurate.

Appendices to this Final Argument. A copy of the live spreadsheet has also been filed, and it includes any additional tables and charts that have been included in submissions that are based on that analysis.[18]



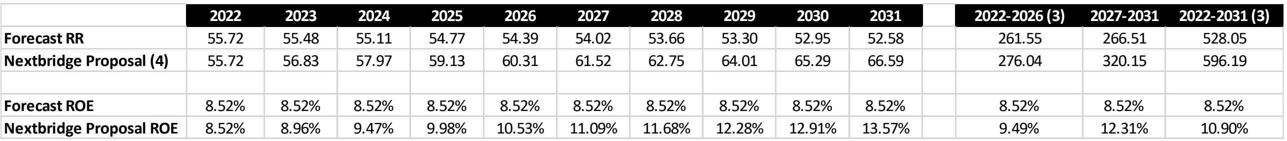
**SEC Analysis (Cost of Service vs. NB RCI Proposal)**

| | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | | TOTAL |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | | |
| **Capital Related RR** | | | | | | | | | | | | |
| Rate Base ($M) | 770.4 | 763.9 | 755.3 | 746.7 | 737.9 | 728.8 | 719.8 | 711.1 | 702.4 | 693.3 | | |
| | | | | | | | | | | | | |
| Cost of LT Debt ($M) (1) | 13.85 | 13.73 | 13.58 | 13.42 | 13.26 | 13.10 | 12.94 | 12.78 | 12.63 | 12.46 | | |
| Cost of ST Debt ($M) (1) | 0.85 | 0.84 | 0.83 | 0.82 | 0.81 | 0.80 | 0.79 | 0.78 | 0.77 | 0.76 | | |
| Return on Equity ($M) (1) | 26.26 | 26.03 | 25.74 | 25.45 | 25.15 | 24.84 | 24.53 | 24.24 | 23.94 | 23.63 | | |
| *Total Cost of Capital* ($M) | 41.0 | 40.6 | 40.1 | 39.7 | 39.2 | 38.7 | 38.3 | 37.8 | 37.3 | 36.9 | | |
| | | | | | | | | | | | | |
| Depreciation ($M) | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | | |
| Income Taxes ($M) | 0.6 | 0.6 | 0.6 | 0.6 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | | |
| | | | | | | | | | | | | |
| **Total Capital RR ($M)** | 50.8 | 50.4 | 50.0 | 49.5 | 49.0 | 48.6 | 48.1 | 47.6 | 47.2 | 46.7 | | |
| | | | | | | | | | | | | |
| **OM&A** | | | | | | | | | | | | |
| OM&A ($M) (2) | 4.9 | 5.0 | 5.1 | 5.2 | 5.3 | 5.5 | 5.6 | 5.7 | 5.8 | 5.9 | | |
| | | | | | | | | | | | | |
| ***Total Annualized RR ($M)*** | 55.7 | 55.5 | 55.1 | 54.8 | 54.4 | 54.0 | 53.7 | 53.3 | 53.0 | 52.6 | | **542.0** |
| | | | | | | | | | | | | |
| ***April 1, 2022 Effective Date RR ($M) (3)*** | 41.8 | 55.5 | 55.1 | 54.8 | 54.4 | 54.0 | 53.7 | 53.3 | 53.0 | 52.6 | | **528.1** |
| | | | | | | | | | | | | |
| ***NB Proposal Annualized RR ($M)*** | 55.7 | 56.8 | 58.0 | 59.1 | 60.3 | 61.5 | 62.8 | 64.0 | 65.3 | 66.6 | | **610.1** |
| | | | | | | | | | | | | |
| ***NB Proposal April 1, 2022 Effective Date ($M)*** | 41.8 | 56.8 | 58.0 | 59.1 | 60.3 | 61.5 | 62.8 | 64.0 | 65.3 | 66.6 | | **596.2** |

(1) Cost of capital parameters fixed for term. Numbers from application.
(2) Assumed annual OM&A increase of 2% to match NB inflation number
(3) Assumed April 1, 2022 effective date as proposed by NB, 2022 RR included at 9/12th of year

v.2

***2.2.3*** The analysis shows that over the 9-year and 9-month term NextBridge proposes to collect a base revenue requirement of $596.2M, whereas its costs will be only $528.1M. This results in a total expected over-collection over the plan term of $68.1M or 13%. Since the forecast costs are decreasing annually, and NextBridge's proposal is to <u>increase</u> the revenue requirement annually by 2%, the gap between the two amounts increases over time.



| | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | | 2022-2026 (3) | 2027-2031 | 2022-2031 (3) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Forecast RR** | 55.72 | 55.48 | 55.11 | 54.77 | 54.39 | 54.02 | 53.66 | 53.30 | 52.95 | 52.58 | | 261.55 | 266.51 | 528.05 |
| **Nextbridge Proposal (4)** | 55.72 | 56.83 | 57.97 | 59.13 | 60.31 | 61.52 | 62.75 | 64.01 | 65.29 | 66.59 | | 276.04 | 320.15 | 596.19 |
| | | | | | | | | | | | | | | |
| **Forecast ROE** | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | | 8.52% | 8.52% | 8.52% |
| **Nextbridge Proposal ROE** | 8.52% | 8.96% | 9.47% | 9.98% | 10.53% | 11.09% | 11.68% | 12.28% | 12.91% | 13.57% | | 9.49% | 12.31% | 10.90% |

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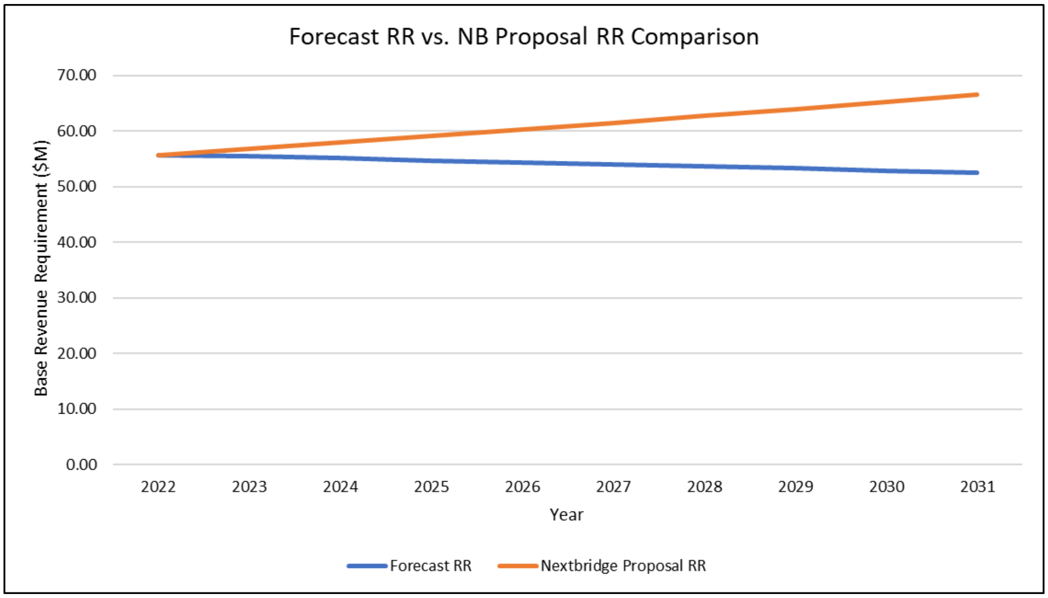
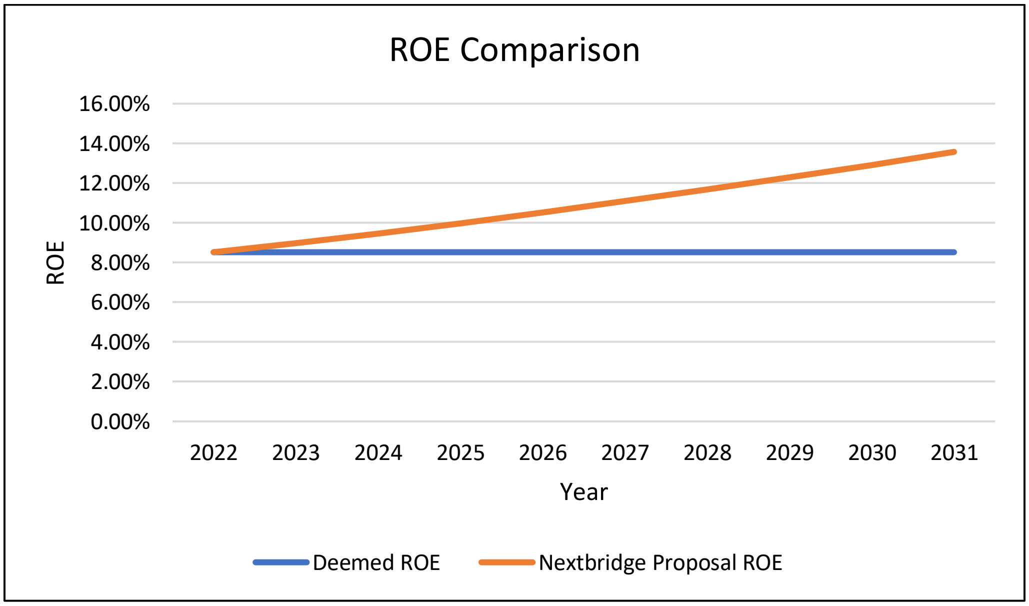
[18] See SEC_NextBridge_Arg_Analysis_20210427.xls



*2.2.4* Based on the forecast costs included in this analysis, NextBridge will earn above the 8.52% deemed ROE included in its 2022 base rates. Over time, as its costs decrease but its proposed revenue requirement increases, its ROE will increase every year, and it will substantially over-earn. By 2031, SEC forecasts that NextBridge will earn an ROE of 13.57%.



*2.2.5* ***NextBridge's Unfounded Objections.*** At the hearing, NextBridge objected to the assumptions included in SEC's analysis. Those objections are unfounded. The assumptions are reasonable and consistent with Board guidance, as set out below.

***2.2.6*** First, NextBridge did not agree that it was appropriate to maintain the cost of capital parameters through the entire rate term.[19] SEC disagrees, since that it is entirely consistent with Board's expectations for rate-setting in both Custom IR and all other rate-setting approaches.

***2.2.7*** The OEB Handbook on Utility Rate Applications is clear that "the general expectation is that the cost of capital parameters will remain unchanged throughout the rate-setting term, typically 5-years."[20] This is also what has occurred in practice. For example, the Board has approved, for both Hydro One (both transmission and distribution) and Toronto-Hydro, Custom IR frameworks which build into the framework for each year cost of capital and debt parameters that are the same as those in the initial base year.[21]

***2.2.8*** NextBridge does not get to have a rate-setting framework that ensures it over-earns as compared to the deemed rate set in the initial rebasing year. This is true even if the rate may be considered relatively low as compared to the historical levels. NextBridge is no different from any utility who had or will have their rates rebased for 2020, 2021 and 2022 (the year NextBridge's rates will be effective).

***2.2.9*** While the Board's deemed current cost of capital rates may be at historic lows relative to the last decade, NextBridge proposes using the Board's 2020 parameters, that were issued before the COVID-19 pandemic began, and not the more recent 2021 parameters, which are lower.[22]

***2.2.10*** Second, NextBridge did not agree with SEC's assumption regarding OM&A costs post 2022. For the purpose of the analysis, SEC assumed that it would increase annually at NextBridge's proposed 2% inflation rate. In its evidence, and at the oral hearing, it provided several cost pressures which it says it will need to manage within its proposed rate plan, above an OM&A budget increasing at inflation.[23] This is what Ms. Tidmarsh referred to as "death by a thousand

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[19] Tr.1, p.70

[20] Handbook for Utility Rate Applications, p.26, Appendix C, p.iii; See also, p.26, "…the OEB does not expect to address annual rate applications for updates for cost of capital….". See also *Decision and Order* (EB-2019-0082), April 23 2020, p.149 "This structure and the parameters will remain in place for the 2020 to 2022 term, consistent with the expectations set out in the OEB's Rate Handbook."

[21] *Decision and Order* (EB-2019-0082), April 23 2020, p.149; *Decision and Order* (EB-2018-0165) December 19 2019, p.151 *Decision and Order* (EB-2017-0049), March 7 2019, p.38

[22] Letter from the Registrar, Re: 2021 Cost of Capital Parameters, November 9 2020 (K1.2, p.93)

[23] Tr.1, p.82-83, 121-149; Interrogatory Response OEB Staff #4, p.1-2

cuts of our OM&A budget".[24]

***2.2.11*** SEC submits the identified cost pressures are exaggerated. In fact, they are more accurately categorized as risks that, if they materialize in a significant quantity, may (without any offsetting savings in other aspects of the budget) increase the OM&A budget annually at amounts more than inflation.

***2.2.12*** Regardless, NextBridge's own target is not to have its total OM&A costs increase at an amount above inflation, or even at inflation. It is to keep the amount flat over-time. Its proposed target for its OM&A metric on its scorecard is that those costs remain flat through the entire term of the plan. [25]

***2.2.13*** As part of its proposed scorecard, NextBridge proposed an OM&A per kilometre metric.[26] The target for that metric remains the same for each year through to the end of the plan in 2031.[27] Since the line does not change in size over the term, this means it expects its total OM&A budget to remain the same. Ms. Tidmarsh confirmed this during the oral hearing, testifying that "NextBridge for its OM&A cost, which is the entire bucket, will endeavor to keep it flat, and so -- and that may require us to seek some cost savings somewhere else…"[28] Mr. Meyers could not be clearer. He commented that "we are setting very aggressive targets, and at the same time, you know, <u>we're confident that we can keep this O&M budget at the 4.94 million that we projected over that 10-year period</u>." [emphasis added][29]

***2.2.14*** Regardless of NextBridge's own targets, allowing OM&A cost growth equal to inflation is not just reasonable, but generous. Customers expect that costs should increase at no more than the rate of inflation, and in fact, the Board expects utilities to have prices increase at an amount below that to incent productivity through a stretch factor. SEC notes that for similar recent Custom IR applications, the Board has approved OM&A increases at amounts below inflation

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[24] Tr.1, p.145

[25] Interrogatory Response OEB Staff #59(c) (K1.2, p.61)

[26] D-1-1, p.1

[27] Interrogatory Response OEB Staff #59(c) (K1.2, p.61)

[28] Tr.1, p.151

[29] Tr.1, p.151

when stretch factors are applied.[30] The Board's traditional I-X approach recognizes that inflation should be the upper bound. It allows rates or costs to increase at inflation minus a stretch factor.

### 2.3 ***Productivity and Stretch Factor***

***2.3.1*** NextBridge has proposed a 0% X-Factor made up of both a 0% productivity factor and a 0% stretch factor.

***2.3.2*** ***Productivity Factor***. NextBridge relies on the findings in Hydro One Sault St. Marie's ("Hydro One SSM") rate framework application, where the Board found that the expert evidence was that there was no expected increased productivity in the transmission sector.[31]

***2.3.3*** SEC does not take issue with NextBridge's use of a 0% productivity factor considering the Board's past findings in the Hydro One SSM proceeding.[32] At the same time, the findings in that proceeding, and the reports that underlie them, are not entirely applicable to this case. The Total Factor Productivity ("TFP") analysis undertaken in that proceeding was on a total cost basis, and those studies reflected actual spending by peer group companies that are undertaking significant annual capital work.[33] They are not single asset utilities. In contrast, the evidence in this proceeding is that NextBridge forecasts needing very minimal capital expenditures during the plan term since its assets are new. The growth in costs, if any, is coming from OM&A.

***2.3.4*** ***Stretch Factor.*** SEC does not agree with NextBridge that a 0% stretch factor is appropriate. NextBridge argues that its proposal is appropriate, since the stretch factor is "typically imposed on utilities that under-perform their peers in order to bring under-performing utilities into line:

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[30] See for example, *Decision and Order* (EB-2017-0049), March 7, 2019, p.32, "For OM&A, Hydro One is expected to manage within an increase of less than inflation (I – X) each year, regardless of its forecast costs."

[31] Argument-in-Chief, p.14, referencing *Decision and Order* (EB-2018-0218), June 20, 2019, p.19

[32] Similar evidence was filed in the context of Hydro One's 2020-2022 Custom IR Application and both experts recommended a 0% productivity factor. In the Board's decision it required Hydro One to apply a 0.3% X-Factor, and did not explicitly state that this was reflective only of a stretch factor component although the language does suggest that it is (See *Decision and Order* (EB-2019-0082), April 23, 2020, p.27, 33).

[33] See for the list of peer utilities in benchmarking sample in the PSE Report (EB-2018-0218, Exhibit D-1-1, Attachment 1, p.22).

the greater the under-performance, the higher the stretch."[34] NextBridge's understanding is incorrect.

***2.3.5*** The Board has consistently said that a stretch factor "is intended to reflect the incremental productivity gains that firms are expected to achieve under IR and is a common feature of IR plans."[35] Under the Board's approach to setting a stretch factor, while greater relative under-performance usually means a higher reduction, only significant over-performers, measured as total costs greater than 25% below predicted costs, have no stretch factor applied.[36] Even an average performer (+/- 10% expected costs), receives a stretch factor at the mid-point (0.3%) of the Board's 0% to 0.6% range.[37]

***2.3.6*** SEC does not dispute that there is limited, if any, productivity that can be achieved with respect to the capital-related revenue requirement, as NextBridge expects to do very minimal capital work during the plan term.[38] The situation is different with respect to OM&A, where there is an ability, and there should be an expectation that it will be able to find efficiencies over time. NextBridge appears to agree. Its own evidence is that its target is to keep OM&A flat during the plan term.[39]

***2.3.7*** NextBridge's reliance on the Charles River Associates ("CRA") benchmarking evidence as confirmation that its performance is superior to other transmitters is also misplaced. As discussed in greater detail in section 3.6, while the CRA benchmarking evidence shows that on a per kilometer basis its OM&A costs appear to be on the lower end of the range, most of the costs included in the budget do not have a linear relationship to the length of the line. Thus, the results cannot be taken to show that NextBridge's forecast OM&A costs are efficient. Moreover, customers are also not paying rates based on revenue requirement per kilometer of

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[34] Argument-in-Chief, p.15

[35] Report: Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach (October 18, 2012), p.17, citing Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributor, (July 14, 2008), p.12

[36] Report of the Board: Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors, November 21, 2013 (corrected on December 4, 2013), p.21

[37] Report of the Board: Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors, November 21, 2013 (corrected on December 4, 2013), p.21

[38] Tr.1, p.48-49; B-1-7, Table 1(K1.2, p.46); Interrogatory Response OEB Staff #34(b) (K1.2, p.48)

[39] Tr.1, p.151; Interrogatory Response OEB Staff #59(c) (K1.2, p.61)

the transmission line. The metric is not relevant as a measure of expected performance from the customers' perspective.

*2.3.8* The inclusion of a 0% stretch factor also inconsistent with the Rate Handbook, which states that for Custom IR applications, "expected productivity gains will be explicitly included in the rate adjustment mechanism."[emphasis added][40] The Board also said that "[g]iven a utility's ability to customize the approach to rate-setting to meet its specific circumstances, the OEB would generally expect the custom index to be higher, and certainly not lower, than the OEB-approved X factor for Price Cap IR (productivity and stretch factors) that is used for electricity distributors."[emphasis added][41]

## 2.4 ***Cost Pressures Are Overstated and Simply Represent Regular Business Risks***

*2.4.1* NextBridge has pointed to a number of cost pressures that it expects to have to manage during the IR term. In its view, these are reasons why it is appropriate for the Board to approve a proposed 2% annual increase, even though it has a declining rate base.

*2.4.2* Those cost pressures, however, are for the most part simply the normal business risks that a transmission utility is expected to operate within, and in any case, are accounted for within the 2022 base OM&A budget. SEC submits that a closer examination of the risks identified demonstrates that these risks are overstated, and their cost impact, if they do occur, can be managed within an OM&A budget increasing at inflation, less a stretch factor.

*2.4.3* ***Hydro One/SuperCom Agreement.*** NextBridge argues that as the Hydro One/SuperCom Service Level Agreement ("SLA") is not a fixed price contract, but activity based, as the activity levels change over time so will the total costs.[42] This is correct, but it assumes the Hydro One/SuperCom level of activity will not only increase over time, but at a rate higher than the assumed level of inflation. There is no evidence that this will be the case. While it is very possible that in any given year, more work may be done under the SLA than expected, in other years there will be less.

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[40] Handbook for Utility Rate Applications, p.24

[41] Handbook for Utility Rate Applications, p.26

[42] Interrogatory Response OEB Staff #4(b), p.2 (K1.2, p.59)

***2.4.4*** Further, one would expect that, as Hydro One/SuperCom gains experience maintaining the line, they will become more efficient in their work.[43] Additionally, even though the agreement is activity based, the time and materials are fixed, and do not escalate during the initial contract length (3 years).[44] So, at minimum in those first 3 years of the term, the assumed increase in the budget for this activity of 2% is actually higher than the expected costs.

***2.4.5*** ***NEET Agreement.*** NextBridge relies on the fact that its contract with NextEra Energy Transmission, LLC ("NEET') for labour services will likely increase at an average rate of 3%, higher than its assumed rate of inflation of 2%.[45] Assuming that this is correct, as the draft SLA simply refers to these as pass-through costs[46], it raises the question of how reasonable such an increase is, considering it is 50% higher than the assumed inflation rate, and being undertaken with a related party. Contrary to NextBridge's view, the NEET work was not undertaken by a truly competitive procurement process (discussed further in section 3.6).[47] Regardless, the impact of any 3% increase is limited to the 34% of the OM&A budget that is covered by the NEET agreement.[48]

***2.4.6*** ***Managing Right of Way Costs & Other Potential O&M Cost Increases.*** NextBridge argues that they may have vegetation management and other O&M cost increases that would not be covered by an inflation increase in the OM&A budget.[49] SEC submits these risks are no different than any other utility whose rates are set by the Board. NextBridge has provided no evidence that these cost increases are *likely* to occur, and that any increase will be above their assumed inflation amount over the plan term. In fact, NextBridge's own evidence is that it has built into its 2022 base year OM&A budget $170,000 to deal with potential O&M issues that may arise, that it does not specifically foresee.[50]

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[43] Tr.1, p.117

[44] Tr.1, p.118

[45] Tr.1, p.123

[46] Undertaking J3.5

[47] Tr.3, p.83-85

[48] Undertaking JT1.1 notes that the NEET agreement covers $1.7M of the total $4.94M OM&A budget.

[49] Interrogatory Response OEB Staff. #4(b), p.2 (K1.2, p.59)

[50] Tr.1, p.91,

***2.4.7*** ***Extreme Weather Events and Unexpected Damage from Right-of-Way Users and Wildlife.*** NextBridge also believes that it will be challenged by the costs of local extreme weather events. Insofar as the events, either extreme weather or third-party caused damage, are material and cannot be absorbed within the O&M budget, they would likely meet the definition of a Z-Factor, for which NextBridge would be eligible for recovery of the costs.[51] If they are immaterial, then they are the type of costs that should be absorbed within the OM&A budget, which also includes amounts budgeted for these types of events, in any case.

***2.4.8*** Mr. Meyers testified that NextBridge, based on NextEra's experience with transmission across Canada and the US, considered costs related to weather events in determining its overall 2022 OM&A budget. [52] The evidence was also that NextBridge had consulted with Hydro One regarding weather and lighting, as Hydro One's own transmission line parallels much of the East-West Tie Line. Ms. Tidmarsh remarked that it used Hydro One's data in building its OM&A budget, and they themselves are knowledgeable since they have been "doing this project for eight years and we've seen a lot of the weather events."[53] Similarly, regarding right-of-way damage, Mr. Meyer testified that this is already considered in their base OM&A budget as "this is rolled up as part of the overall maintenance mitigation costs."[54]

***2.4.9*** ***New First Nations Reserve Land added & NERC compliance changes***. NextBridge cites these two potential cost increases over the plan. SEC notes that the entire budget for land rights payments for crossing First Nations reserves is less than $60K in 2022[55], so any new land that may be added during the term plan, which is not a regular occurrence, will not be large. Regarding NERC standard changes[56], they are also likely to have a small impact on the OM&A budget, but in the scenario that change is significant and the cost material, it would likely be

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[51] Tr.1, p.88,142;

[52] Tr.1, p.143-144

[53] Tr.2, p.9-10

[54] Tr.1, p.149

[55] F-4-1, p.2. Table 1 (K1.2, p.65). Total property taxes and rights payment budget is $60K, whereas property taxes portion is forecast to be $4.9K (See Tr.2, p.164).

[56] Interrogatory Response OEB Staff #59(c) (K1.2, p.61)

the type of cost eligible for a Z-Factor treatment.[57]

***2.4.10*** ***Rising Income Tax Expenses.*** NextBridge claims that as its capital cost allowance declines it will have a rising income tax expense during the plan term.[58] This is incorrect. NextBridge's own evidence is that it will be paying only OCMT through the plan term instead of regular corporate tax, because of tax losses that will have been generated primarily in 2022 due to available accelerated CCA deduction.[59] Furthermore, like regular corporate income tax, any changes in OCMT during the plan term will primarily be a function of the revenue it receives through the rate framework. If the Board approves a framework with the revenue requirement declining annually to reflect its actual cost structure, then the OCMT payable will also decline annually.[60]

***2.4.11*** ***Debt Costs.*** At the hearing, NextBridge stated it expects actual debt costs will increase over the plan term, caused by higher debt rates than those ultimately included in base rates, and trued-up through its proposed Debt Rate Variance Account ("DRVA").[61] As SEC understands NextBridge's view, debt rates are likely to increase over-time.[62]

***2.4.12*** NextBridge's evidence is that it plans to issue debt in various tranches to match its actual capital structure during the plan term.[63] Because of its decreasing rate base, it will require less actual debt over time to maintain the deemed capital structure. To accomplish this, NextBridge plans to acquire debt in various tranches with varying term lengths.[64] SEC agrees this is a prudent strategy but considering that its rate base is decreasing at approximately 1% a year[65], and at the

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[57] Tr.1, p.150

[58] Interrogatory Response OEB Staff #4(b), p.2 (K1.2, p.59)

[59] Interrogatory Response SEC #12 (K1.2, p. 45); Tr.1, p.135-136

[60] K1.2, p.59, See line 47-49. As proposed, NextBridge's RCI will result in higher income tax costs but only because it is expected to over-earn, which will result in the requirement to pay higher tax. Forecast over-earning is not a good reason to increase the revenue requirement nor are they true cost pressures.

[61] H-1-1, p.5; Tr.1, p.29; G-2-2, p.1

[62] Tr.1, p.94

[63] Tr.1, p.67; Tr.1, p.95-96

[64] Tr.1, p.67

[65] See Appendix B, change in Line 20 year-over-year. See also the annual average depreciation rate is 1.2% (Tr.1, p.49-50; F-11-1, p.2 (K1.2, p.36).

end of the term plan it will be 10% less than 2022 levels[66], the vast majority of the long-term debt (approximately 90%) should be at least greater than 10 years to lock in the current relatively low rates.

***2.4.13*** Oddly, NextBridge testified that "very little of it is going to have really long terms" of "ten or more years".[67] This makes little sense and is not a prudent way to manage debt costs when rates are as low as they are. SEC submits NextBridge should be locking in as much debt as possible at terms of at least 10 years, if not much longer. It should minimize its debt that is less than 10 years to the amount required to match its capital structure. Having most of your debt in tranches below 10 years is imprudent, based on the rate of the rate base decline and the current interest rates environment. It is also consistent with proper corporate finance, in which long term assets are financed by long-term debt, and short-term needs are financed by short term debt.

***2.4.14*** On this basis, SEC questions if their high-level description of their approach provided during the oral hearing is what will end happening. When asked, NextBridge said it did not have a formal or informal plan that maps out, with some level of specificity, their debt tranche strategy at this time.[68]

***2.4.15*** The reason this matter is that if NextBridge pursues a prudent strategy as described above, with 90% of its long-term debt having durations longer than the plan term, its actual weighted average long-term debt rate throughout the plan term will be only minimally different from what will be included in its 2022 base rates (or as updated in the DRVA).

## 2.5 ***Proposed Rate Framework Does Not Meet Test for Just and Reasonable Rates***

***2.5.1*** In approving any rate framework, the Board must ensure that it will result in rates, or in this case the revenue requirement, that are just and reasonable.[69] NextBridge's proposed rate-setting framework essentially guarantees that it will over-earn, even if it has abysmal

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[66] See Appendix B, change in 2031 Total Avg. NBV versus 2022 (Line 20).

[67] Tr.1, p.96

[68] Tr.1, p.99

[69] Handbook for Utility Rate Applications, p.1,5; OEB Act, p.78(3)

performance. This is legally impermissible.

***2.5.2*** The Supreme Court has interpreted the legal requirement as rates that "under the circumstances, would be fair to the consumer on the one hand, and which, on the other hand, would secure to the company a fair return for the capital invested".[70] In *Ontario Power Generation* v. *Ontario Energy Board*, it held that this means the utility must "over the long run, be given the opportunity to recover, through the rates it is permitted to charge, its operating and capital costs ("capital costs" in this sense refers to all costs associated with the utility's invested capital)."[71] At the same time, the Supreme Court noted that "this of course does not mean that the Board must accept every cost that is submitted by the utility, nor does it mean that the rate of return to equity investors is guaranteed".[72]

***2.5.3*** The Board allows utilities to apply under multiple rate-setting approaches, but common to each is that, "[u]tilities are expected to demonstrate sustainable improvements in their efficiency and in doing so will have the opportunity to earn a fair return."[73] This means that an approved rate-framework should target that a utility should earn its approved ROE, if it is able to demonstrate a sufficient level of efficiencies over its rate-setting term. This is the incentive aspect of incentive regulation.

***2.5.4*** Just as it would not be just and reasonable to approve a rate-setting framework that does not allow a utility the opportunity to recover a fair rate of return on its invested capital, it similarly is not just and reasonable to approve a rate-setting framework that structurally ensures that it will over-earn. It will over-earn in each year beginning in 2023. By 2031, SEC forecasts its ROE will be 13.57%. This is more than 500-basis points above the deemed rate it proposed to include in its 2022 base revenue requirement (8.52%).

***2.5.5*** None of this is to say that utility should have no opportunity to over-earn during its rate-setting plan. It should have that opportunity, but only if it is able to find greater effectiveness and

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[70] *Ontario (Energy Board) v. Ontario Power Generation Inc.*, 2015 SCC 44, para.15, citing *Northwestern Utilities Ltd. v. City of Edmonton*, [1929] S.C.R. 186, p.192-93

[71] *Ontario (Energy Board) v. Ontario Power Generation Inc.*, 2015 SCC 44, para.16

[72] *Ontario (Energy Board) v. Ontario Power Generation Inc.*, 2015 SCC 44, para.17

[73] Handbook for Utility Rate Applications, para.3

sustainable improvements than would normally be expected of them. It can over-earn if it over-performs.

***2.5.6*** NextBridge's proposed rate-setting framework essentially guarantees that it will over-earn even if it has abysmal performance. This is not consistent with good ratemaking, is contrary to the Board's policies and regulatory approach, and does meet the legal requirement that rates must be just and reasonable.

## 2.6 ***300-Basis Point Off-Ramp Does Not Solve the Problem***

***2.6.1*** When presented with SEC's analysis that showed that under its proposed rate framework it will likely over-earn in each year after 2022, NextBridge kept referring to the Board's generic 300-basis points off-ramp as the main reason that while SEC's analysis demonstrates that, it may over-earn, it will not be as bad as shown. Ms. Walding said that NextBridge does not actually expect to earn the revenues that they are seeking approval for in this application, "because we would fully expect to have a rate review and have our rates reset if we earned outside of that debt (sic) band."[74]

***2.6.2*** NextBridge has mischaracterized both the purpose and the effect of the Board's generic 300-basis point off-ramp.

***2.6.3*** The intent of the Board's generic 300-basis point off-ramp, which is symmetrical, is to act as an 'emergency break' on a rate-setting plan because an extreme and unexpected event has occurred that cannot effectively be addressed through the existing mechanisms in a rate-setting plan.[75] If the Board is able to forecast a utility will likely to hit the 300-basis point off-ramp, then there is something inherent in the structure of the proposed rate framework that is unreasonable.

***2.6.4*** Even if a utility hits the 300-basis point off-ramp, that does not necessarily require the Board to actually undertake a review, let alone making any adjustment to rates or the revenue requirement. The threshold simply is the point in which "a regulatory review may be triggered"

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[74] Tr.1, p..73-74, See also Tr.2, p.44

[75] Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors (July 14, 2008), p.37-40

[emphasis added].[76]

***2.6.5*** If the Board does wish to *consider* making an adjustment to NextBridge's revenue requirement during the plan term upon the threshold being met, there is a necessary lag before it is able to make any change. By way of a recent example, the Board on its own motion established a variance account to capture any earnings OPG has above the 300-basis points in 2021, as a result of achieving an ROE above the 300-basis threshold in 2019.[77] The delay is a result of the fact the OEB only received the results of OPG's 2019 performance, after the filing of its annual RRR filings in 2020. Since 2020 rates were set in late 2019, there is limited opportunity to make any adjustment before 2021.

***2.6.6*** As a general matter, the Board is limited in its ability to claw back past over-earnings, as that would normally be impermissible retroactive ratemaking. NextBridge's reporting and rate adjustment schedule will be no different than OPG. This means that if they exceed the 300-basis point over-earning threshold as forecast in 2028, the earliest the Board could make any adjustment to its rates would be in 2030.

## 2.7 ***ESM Not An Appropriate Remedy***

***2.7.1*** SEC submits that while it may be tempting to impose an Earning Sharing Mechanism ("ESM") as a way to address the structural deficiencies in NextBridge's rate plan, it is not a sufficient, or an appropriate response.

***2.7.2*** An ESM is meant to share any over-earnings between a utility and customer that may arise over the duration of the rate plan, if the company is able to achieve greater efficiencies than forecast. Traditionally this has been included in many Custom IR plans in which, due to the asymmetry of information that exists between the utility and the regulator, a rate protection mechanism is required to protect against the possibility that forecast costs may be overstated, and/or potential efficiency opportunities understated.

***2.7.3*** Here, the evidence already shows that NextBridge will significantly over-earn based on the

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[76] OEB Rate Handbook, p.28; See also Report of the Board: Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach (October 18, 2012), p.11

[77] Notice of Proceeding and Accounting Order (EB-2020-0248), November 9 2020, p.1

forecast costs. It would only be appropriate to include an ESM *after* adjustments have been made to the RCI model so that the target ROE is at the deemed level. NextBridge should only be able to over-earn, and either retain some or all of the savings, if it is able to demonstrate greater efficiencies than forecast. An approved rate framework should not be approved with the expectation that there will be over-earnings.

## 2.8 ***SEC Proposal***

***2.8.1*** SEC proposes that in light of the very different drivers of the capital and OM&A costs over the IR term, a two-part approach that adjusts annually the OM&A and capital-related portions of the revenue differently as part of the RCI is the most appropriate method for setting NextBridge's revenue requirement from 2023 to 2031.

***2.8.2*** A traditional I-X RCI framework does not make sense for a utility like NextBridge. Incentive Regulation is designed to decouple revenue from costs, to incent a utility whose costs are increasing to be more productive and efficient by managing within a revenue envelope. It was never meant to allow a utility whose costs are declining to increase its revenues. Doing so destroys all the incentives to operate efficiently.

***2.8.3*** Under SEC's proposed approach, the OM&A would be adjusted annually by a traditional I-X approach, but the capital-related revenue requirement would not be inflated at all, and a negative adjustment factor would be applied to reflect the declining rate base and thus declining costs. This reflects the starkly different drivers of costs through the rate plan related to these two categories.

***2.8.4*** The capital-related revenue requirement (cost of capital, depreciation and incomes taxes) decreases in fact during the plan term, and except for very minor capital additions expected between 2023 and 2031[78], the capital is not impacted by inflation or any type of potential productivity. These are essentially fixed costs.

***2.8.5*** This differs from the OM&A portion of the revenue requirement, which is impacted by inflation and productivity.

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[78] Interrogatory Response OEB Staff #34(b) (K1.2, p.48)

**Revenue Requirement = OM&A Revenue Requirement + Capital-Related Revenue Requirement Adjustment**

*2.8.6* ***OM&A.*** SEC proposes that the OM&A portion of the revenue requirement be increased annually by a traditional I-X approach. Instead of setting a fixed inflation factor of 2% for each of the 9 years where an RCI adjustment is to be made, the inflation amount would change based on the inflation factor for transmission issued by the Board annually. This ensures that NextBridge gets the benefit of an annual adjustment that better reflects an actual economy-wide inflation rate.

*2.8.7* SEC believes an appropriate stretch factor component of the X-Factor is 0.3%, the midpoint of the Board's 0% to 0.6% range. This reflects the expectations of both the Board and customers' that there should be continuous improvement in NextBridge's operations over time, and that should be reflected in a savings provided explicitly through the annual rate adjustment mechanism, as is the Board's standard practice. It is also consistent with the Board's decision in Hydro One's recent transmission Custom IR application, where it found that a 0.3% stretch factor was appropriate on the basis that "that a revenue cap adjustment that allows Hydro One to escalate its revenue requirement by the full amount of inflation is not consistent" with the "performance-based approach to regulation" outlined in the Rate Handbook.[79]

**OM&A Revenue Requirement = Previous Years Approved OM&A x (1+OM&A Adjustment)**
**OM&A Adjustment = I-X**
**OM&A Adjustment = OEB's Annual Inflation Factor For Transmission Applications – Productivity Factor of 0.3%**

*2.8.8* ***Capital-Related Revenue Requirement.*** SEC proposes that the capital-related revenue requirement be adjusted annually downwards by a Capital Adjustment Factor.

**Capital-Related Revenue Requirement Adjustment = Previous Years Approved Capital-Related RR x (1 - Capital Adjustment Factor)**
**Capital Adjustment Factor = 0.09 (0.93%)**

*2.8.9* The proposed Capital Adjustment Factor would be set at 0.9%, which is based on the SEC's analysis and reflects the average yearly reduction in the forecast capital-related revenue

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[79] *Decision and Order* (EB-2019-0082), April 23 2020, p.33

requirement (shown below). The capital-related revenue requirement used in the analysis includes not just the impact of the 2022 rate base, but also the addition of the $4.05M of capital expenditures between 2023 and 2031.[80]

| ***Capital Adjustment Factor*** | **2022** | **2023** | **2024** | **2025** | **2026** | **2027** | **2028** | **2029** | **2030** | **2031** |
|---|---|---|---|---|---|---|---|---|---|---|
| **Capital-Related RR ($M)** | 50.78 | 50.44 | 49.97 | 49.53 | 49.05 | 48.57 | 48.09 | 47.62 | 47.16 | 46.67 |
| **Annual Reduction (%)** | | -0.67% | -0.92% | -0.89% | -0.98% | -0.97% | -0.98% | -0.97% | -0.97% | -1.04% |
| **Average** | | | | | | | | | | -0.93% |

***2.8.10*** ***Rate Adjustment Summary.*** Based on this two-part approach, the forecast ROE based on forecast costs while varying slightly from year-to-year, averages the deemed rate of 8.52%. This demonstrates that the proposed approach and adjustment factors are appropriate and ensures that NextBridge has an opportunity to achieve a fair rate of return – the deemed amount built into 2022 base rates, over the duration of the plan.[81]

| ***SEC Proposal*** | **2022** | **2023** | **2024** | **2025** | **2026** | **2027** | **2028** | **2029** | **2030** | **2031** |
|---|---|---|---|---|---|---|---|---|---|---|
| **Split RR (Capital RR - Cap Adj Factor) OM&A (I-X)** | | | | | | | | | | |
| **Capital-Related RR ($M)** | 50.78 | 50.32 | 49.87 | 49.42 | 48.98 | 48.54 | 48.10 | 47.67 | 47.24 | 46.81 |
| **OM&A ($M)** | 4.94 | 5.02 | 5.11 | 5.20 | 5.28 | 5.37 | 5.47 | 5.56 | 5.65 | 5.75 |
| **Total RR ($M)** | ***55.72*** | ***55.35*** | ***54.98*** | ***54.62*** | ***54.26*** | ***53.91*** | ***53.57*** | ***53.23*** | ***52.89*** | ***52.56*** |
| **ROE (%)** | 8.52% | 8.48% | 8.49% | 8.48% | 8.50% | 8.51% | 8.52% | 8.53% | 8.55% | 8.57% |

***2.8.11*** It also provides an incentive for NextBridge to drive the efficiencies it is already targeting. Unlike NextBridge's proposed rate framework, SEC's proposal aligns with its forecast capital-related costs, while providing the company with an opportunity for its shareholder to benefit, if it is able to drive superior performance in excess of a stretch factor, including anything close to its own target to maintain a flat OM&A budget.

***2.8.12*** ***Alternative Approach.*** If the Board does not want a two-part approach, and prefers one single adjustment to the revenue requirement, SEC proposes an annual RCI that is based on adjusting the previous years approved revenue requirement by inflation minus a stretch factor minus an Adjustment Factor (I-X-Adjustment Factor). In many ways this approach is similar to the RCI formula approved for Hydro One for both transmission and distribution which includes a Capital Factor to recover approved amounts that would not be recovered by the I-X

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[80] Tr.1, p.48-49; B-1-7, Table 1(K1.2, p.46); Interrogatory Response OEB Staff #34(b) (K1.2, p.48)

[81] The average ROE over the 2022-2031 rate term is 8.52% (See Appendix C, Row 13).

adjustment.[82]

**Revenue Requirement = Previous Year Approved Revenue Requirement X (1+ I-X-Adjustment Factor)**
**Revenue Requirement = Previous Year Approved Revenue Requirement X (1+0.02-0.003-0.0235)**

***2.8.13*** The detective Adjustment Factor to ensure NextBridge earns its deemed ROE over the rate plan would be 2.35%.[83]

| ***Alternative Appraoch*** | **2022** | **2023** | **2024** | **2025** | **2026** | **2027** | **2028** | **2029** | **2030** | **2031** |
|---|---|---|---|---|---|---|---|---|---|---|
| **Total RR (I-X-Adj Factor)** | | | | | | | | | | |
| ***Total RR*** | ***55.72*** | ***55.36*** | ***55.00*** | ***54.64*** | ***54.29*** | ***53.93*** | ***53.58*** | ***53.23*** | ***52.89*** | ***52.54*** |
| ***ROE*** | 8.52% | 8.49% | 8.49% | 8.49% | 8.50% | 8.52% | 8.53% | 8.54% | 8.55% | 8.56% |

***2.8.14*** SEC notes that if the Board were to adopt this alternative approach, it must fix the inflation factor and stretch factor for the entire term. This is because the Adjustment Factor of 2.35% is calculated based on an inflation factor of 2% and a stretch factor 0.3%. While in the Hydro One context the inflation factor is updated each year, due to NextBridge's circumstances this would result in potential significant over (or under) earnings. The reason for this is that Hydro One has significant capital additions each year and an increasing rate base, and insofar as there is a difference in the annual Board inflation number and the assumed rate when the capital factor is determined, that also impacts Hydro One's capital costs. For example, if the capital factor was based on assumed inflation of 2%, but the Board's updated inflation factor is 2.5%, then it is fair that Hydro One is able to recover the additional amounts across its entire revenue requirement since all costs, capital and OM&A, are impacted by the increase in inflation.

***2.8.15*** For NextBridge this is not the case. Except for the *de minimis* capital expenditures it will incur during the rate term, its capital-related revenue requirement is not impacted by any update to the inflation factor. A higher annual inflation factor compared to the 2% assumed level used to calculate the Adjustment Factor would result in significant over-earnings. Similarly, a lower

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[82] *Decision and Order* (EB-2019-0082), April 23, 2020, p.34-39; *Decision and Order* (EB-2017-0049), March 7, 2019, p.30-33). Toronto Hydro has a similar mechanism approved in its recent Custom IR application but since its proposal was a Price Cap IR, the mechanism to implement is different (See *Decision and Order* (EB-2018-0165), December 19, 2019, p.36-41).

[83] The average ROE for the 2022-2031 term is 8.52% which equals the proposed deemed rate (See Appendix C, Row 20). In calculating the ROE, SEC has assumed that there will be no productivity gained from any aspect of the capital-related revenue requirement.

annual inflation factor compared to 2% used to calculate the Adjustment Factor, would result in significant under-earnings.

***2.8.16*** This is the reason SEC prefers the two-part approach. It allows the two different types of cost components, capital, and OM&A, to be adjusted in a way that specifically reflects the drivers of their respective costs and allows the inflation factor to be updated annually to reflect the changes in the economy.

## 2.9 ***ESM and Rate Term***

***2.9.1*** NextBridge proposes a term of 10 rate years (9 years and 9 months). This is significantly longer than the 5-year period that has previously been approved in any other Custom IR application. SEC does not oppose the length of term, contingent on the Board making significant changes to the annual RCI formula as proposed in these submissions. If the Board gets the numbers right, then the length of the term is not especially important.

***2.9.2*** If the Board does not agree that significant changes should be made to the proposed RCI formula, then the length of term must be shortened to 5 years (4 years and 8 months). This is because, as discussed in section 2.2, the longer the rate term the higher the ROE NextBridge is forecast to achieve due to the increasing gap between the revenue it will collect under its proposed rate framework and its forecast costs. A shorter plan term will allow the Board to re-assess the situation much earlier.

***2.9.3*** While the OEB Handbook does allow terms greater than five years, it has said that "[l]onger terms can be proposed with appropriate mechanisms for consumer protection."[84] NextBridge has not proposed any customer ratepayer protection mechanisms. It has not proposed an ESM on the basis that one is not a requirement of the Board.[85] While it is correct that an ESM is not strictly required for a Custom IR plan, it is a common ratepayer protection mechanism, which is a requirement for plans longer than 5 years. An ESM would be such a mechanism and would ensure that insofar as NextBridge is able to achieve its <u>own</u> target of a flat OM&A throughout the plan term, as opposed to any I-X increase, ratepayers would share in those savings.

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[84] OEB Handbook, p.25

[85] Argument-in-Chief, p.17-18

# 3 2022 BASE REVENUE REQUIREMENT

## 3.1 *Rate Base*

***3.1.1*** NextBridge is seeking approval of a 2022 rate base of $770.4M.[86] This includes forecast construction costs of the transmission line ($737.1M), phase shift costs ($5.33M), its spares strategy ($1.2M), and the previously approved development costs ($31.2M).[87] In addition there is approximately $230K of in-service additions during the year.[88] SEC's concern is not with respect to the quantum or the calculations of the proposed 2022 rate base. However, as discussed below the evidence does not demonstrate that the proposed variance account is required to capture the difference between the forecast and actual construction costs.

## 3.2 *Construction Costs*

***3.2.1*** NextBridge is seeking approval of its forecast construction of $737.1M.[89] The amount remains the best estimate NextBridge has regarding the on-going cost of constructing the transmission line that is forecast to go in-service on March 31, 2022 and is consistent with its on-going reporting to the Board.[90] The forecast amount has remained essentially the same since NextBridge filed its leave to construct application in 2017.[91]

***3.2.2*** SEC does not take issue with the reasonableness of the proposed construction costs of $737.1M.

***3.2.3*** The forecast construction costs are consistent with what was forecast in the leave to construct proceeding. Based on the quarterly updates provided to the Board since that date, the total remains on budget with about 60% having already been spent[92], and 90% currently spent or under contract.[93]

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[86] C-1-1, p.2; Tr.1, p.19

[87] C-2-2, p.1; C-2-3, p.1; C-2-4, p.1; C-2-5, p.1 (K1.2, p.30-34); Tr.1, p.44-47

[88] A-3-1, p.12, Table 3; Tr.1, p.48

[89] C-2-4, p.1 (K1.2, p.32); Tr.1, p.43; Tr.1, p.100

[90] Quarterly EWT Project Progress Report (January 22, 2021), p.32 (K1.2, p.84); Tr.1, p.102; See also Quarterly EWT Project Progress Report (April 22, 2021) filed by NextBridge on April 23, 2021, p.33

[91] *Decision and Order* (EB-2017-0182/194/365), December 20, 2018, p.46 (K1.2, p.76)

[92] Tr.1, p.23

[93] C-2-4, p.4

***3.2.4*** SEC is also comforted by the fact that the most significant component of the construction costs is the work undertaken by its major construction contractor. NextBridge's evidence is that it undertook a competitive procurement process for a general contractor under a fixed-price hybrid engineer, procure and construct ("EPC") contract, and selected Valard Construction ("Valard") for the work.[94] NextBridge's evidence is that, with one exception regarding the change in the in-service date, where the cost increase is being absorbed by the allocated contingency, there have been no change orders under the contract.[95]

***3.2.5*** The only likely material change in costs could be due to the force majeure declaration regarding COVID-19 costs.[96] NextBridge has not been presented with Valard's COVID-19 related costs. NextBridge proposes that if there are any that push the total construction costs above the $737M, that those costs would be recorded in the CCAA.

***3.2.6*** SEC is surprised and concerned that NextBridge has not had any discussions regarding the magnitude of the cost, at least for the purposes of mitigating them.[97] Ultimately, that is a risk that NextBridge will have to deal with in the context of a prudence review of any potential COVID-19 related costs for which it may seek approval at a later date, but it is disconcerting.

***3.2.7*** NextBridge has filed benchmarking evidence from CRA in an attempt to demonstrate the reasonableness of the forecast construction cost.[98] SEC submits that the analysis is of limited value. This is not meant to be a criticism of CRA. The very exercise of comparing a relatively limited number of large transmission projects, based on imperfect information[99], requiring a multitude of adjustments to account for different designs, voltages, circuit sizes, location, terrain, and length, is an exceedingly difficult task.

***3.2.8*** During the leave to construct proceeding Hydro One had forecast that the construction cost for

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[94] C-2-4, p.4; Interrogatory Response Energy Probe #20

[95] Tr.2, p.90

[96] Tr.1, p.110

[97] Tr.1, p.110

[98] B-1-7, Attachment 1

[99] Mr. Russo on behalf of CRA testified that in certain circumstances it had "granular" construction cost information from regulatory filings, in other cases he did not and had to make some assumptions. (See Tr.2, p.146).

its competing Lake Superior Link project was approximately $631M.[100] It is hard not to look at that number in comparison to the NextBridge forecast, which is 17% higher. At the same time, SEC does recognize that Hydro One never ultimately was required to submit a "not to exceed" price[101] and so it is not clear what their final proposal would have been when all the various caveats were removed, which at the time had raised significant doubts about the reliability of its estimate.[102]

## 3.3 *Capital Construction Variance Account*

***3.3.1*** NextBridge has proposed the Construction Cost Variance Account ("CCVA") to capture three separate categories of construction cost variances.[103] First, the general variance between actual versus forecast construction costs.[104] Second, COVID-19 related costs in excess of the forecasted construction costs.[105] Third, the directly related costs associated with construction that extend past the in-service date, such as those related to commitments made as part of the amended Environmental Assessment ("EA"), and the Overall Benefits Permit ("OBP") that are not already accounted for in the construction costs.[106] SEC has a concern with each component of the proposed CCVA.

***3.3.2*** ***General Construction Cost Variances***. SEC submits does not oppose approval of the $737.M construction cost forecast, the Board should reject the creation of the proposed CCVA to record general variances between the actual and the amount approved. The Board does not regularly create symmetrical variance accounts to allow for the true-up of forecast capital costs. Utilities in rate applications forecast costs and, for the most part, are required to live with their forecasts during the rate plan. It is only at their subsequent rebasing application in which the prudence of any variances is considered. Insofar as there is a difference, that is reflected on a going forward basis only. In the interim, the risk (or benefit) is that of the utility.

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[100] *Decision and Order* (EB-2017-0182/194/365), December 20, 2018, p.47

[101] *Decision and Order* (EB-2017-0182/094365), February 1,1 2019, p.5

[102] See EB-2017-0182/194/364, Final Argument of the School Energy Coalition (Public Version) dated October 31, 2019, p.9-16

[103] Tr.1, p.29; H-1-1, p.2-3 (K1.2, p.10-11)

[104] Tr.1, 58-59; H-1-1, p.2-3 (K1.2, p.10-11)

[105] H-1-1, p.2-3 (K1.2, p.10-11)

[106] Tr.1, p.61; H-1-1, p.2-3 (K1.2, p.10-11)

***3.3.3*** If the Board is going to approve such an account, it should be on an asymmetrical basis to protect ratepayers. This is the type of capital related variance account that the Board has regularly approved in the context of Custom IR applications.[107]

***3.3.4*** Generally, symmetrical variance accounts for capital projects are allowed if the project themselves are initiated by a third-party. This has been applied, for example, to road relocation work or traditional system access work, where the utility is at the mercy of a third-party and both the cost and timing of the work is hard to forecast.[108]

***3.3.5*** The proposed construction costs are not of the same type. The project and costs are well known, and the work is underway. NextBridge's own evidence is that "[t]here is no uncertainty around the $737 million of construction costs."[109] Ms. Walding confirmed this, saying that "at this point we don't have uncertainty" and "737 is our best estimate of those costs, and so it's the best estimate that we have right now."[110] In addition, NextBridge points to the fact that it has to-date contracted 90% of the forecast costs.[111]

***3.3.6*** NextBridge's concern appears to be that unforeseen things could happen that will impact their costs.[112] There is undoubtedly a risk that something unforeseen may occur, but that is inherent in any forecast cost ratemaking, and is not unique to NextBridge. In fact, based on the status of the project to date, NextBridge is likely at <u>less</u> risk than other utilities, where they are forecasting out significant capital additions years in advance.

***3.3.7*** On that basis, SEC submits that NextBridge should not be provided with a symmetrical

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[107] See for example the Capital Related Revenue Requirement Variance Account in Toronto Hydro's 2020-2024 Custom IR Application (*Decision and Order* (EB-2018-0165), December 19 2019, p.42-43, 193-195), the Capital In-Service Addition Variance Account in Hydro One's 2018-2022 Distribution Custom IR Application (*Decision and Order* (EB-2017-0049), March 7 2019, p.172-173) and the Capital In-Service Variance Account in Hydro One's 2020-22 Transmission Custom IR application (*Decision and Order* (EB-2019-0082), April 23 2020, p.149, p.172-73).

[108] See for example the Externally Driven Capital variance account approved in Toronto Hydro's 2020-2024 Custom IR application (*Decision and Order* (EB-2018-0165), December 19 2019, p.198)

[109] Interrogatory Response OEB Staff #52(c) (K1.2, p.89); Interrogatory Response OEB Staff #46(b) (K1.2, p.87)

[110] Tr.1, p.104-104

[111] Interrogatory Response OEB Staff #52(d),(e) (K1.2, p.89-90)

[112] Tr.1, p.106

variance account to capture general cost variances related to construction cost**s.**

***3.3.8*** ***COVID-19.*** With respect to COVID-19 related costs, SEC does not take issue with NextBridge recording those amounts in a variance account, but it should do so on the same basis as all other regulated utilities do in Ontario, in the Board's generic Account 1509.

***3.3.9*** NextBridge's rationale seems to be that Account 1509 "is for differences in earnings for transmitters with rates currently in place."[113] In that, NextBridge appears to be referring to the Board's on-going consultation in EB-2020-0133 regarding generic guidelines regarding how cost should be recorded and on what basis recovery should be permitted.

***3.3.10*** On April 13, 2021, the Board issued a letter in that consultation providing guidance that the guidelines that the Board will issue will not apply to among others, greenfield utilities, including NextBridge.[114] The letter did not say that these utilities should not record their COVID-19 related costs in Account 1509, simply that the generic guidelines will not apply to the utilities listed in the Board's letter. Account 1509 is still the appropriate place to record any COVID-19 related costs that NextBridge has incurred in this category. How a future Board will determine what balances, if any, should be disposed of is entirely a different matter.

***3.3.11*** The reason that it is important that these costs be recorded in Account 1509 is it requires NextBridge to specifically segregate out COVID-19 related costs from all other potential amounts. Moreover, it does not presuppose that all NextBridge will need to show is that the amounts are prudent and material to be recovered. Even though the Board's generic guidelines will not apply to NextBridge, that does not mean any of the underlying principles contained within that OEB Staff Proposal, including that of necessity, will not be relevant.[115] But that is properly a question for a future application. At this point, the question is simply where should NextBridge record these costs.

***3.3.12*** ***Post In-Service EA/OBP Related Costs***. SEC does not oppose NextBridge's request for

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[113] Tr.1, p.27, 59; Also, Argument-in-Chief, p.4 40

[114] Letter from the Registrar, Re: Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency (EB-2020-0133), April 13, 2021, p.1

[115] OEB Staff Proposal, Consulting on the Deferral Account – Impacts Arising from the COVID-19 Emergency (EB-2020-0133), December 16, 2020, p.11

variance account treatment for costs that extend past the in-service date, such as those related to commitments made as part of the amended EA and OBP that are in excess of the amount included in its construction budget. SEC submits that these costs should be limited to those that extend past the in-service date, related only to commitments or requirements of the amended EA and/or the OBP, and above those amounts included in the construction budget. SEC agrees with NextBridge that a variance account treatment is appropriate for these amounts, as they are not known with any precision at this time, are driven by third-party requirements, and will likely only be incurred for the first couple years of the rate plan.[116]

***3.3.13*** Where there is disagreement is what variance account should be used to record these amounts. SEC submits these should be included in a separate variance account because at this point the Board is not in a position to determine if any balances should be treated as capital or OM&A. If it is the latter, it differs from the treatment of the other proposed amounts to be recorded in the CCVA. While these amounts may relate to the construction phase, since they will be incurred post in-service, potentially for a few years, it is not clear from an accounting perspective that they should be capitalized. NextBridge's evidence is that these "can be capital costs" but it "really kind of depends a lot on how the regulator views them."[117] SEC submits that since specific costs are not known, the Board is not in a position to determine the appropriate regulatory accounting treatment at this time. On this basis, a separate account is warranted, since the other proposed CCVA costs all relate to construction phase costs incurred before the in-service date of the line and will be capitalized.

## 3.4 ***Depreciation Expense***

***3.4.1*** NextBridge proposes approval of a 2022 depreciation expense of $9.26M.[118] Based on the proposed 2022 rate base, the amounts appear to be correctly calculated and reasonable.

## 3.5 ***Cost of Capital and Debt Rate Variance Account***

***3.5.1*** NextBridge proposes to set the 2022 revenue requirement using the Board's 2020 cost of capital parameters, issued in the fall of 2019, even though they will be two years out of date by

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[116] Tr.1, p.61

[117] Tr.1, p.65

[118] F-11-1, p.1

the time the line goes in-service.[119]

***3.5.2*** SEC submits that NextBridge should be required to update its cost of capital parameters amount built into the 2022 base revenue requirement to either the available 2021 or, even better, that it be a placeholder until the Board issues its 2022 parameters. This is required under the Board's Filing Requirements. [120]

***3.5.3*** The 2022 cost capital parameters will be issued the fall of and sufficiently before NextBridge's revenue requirement is added to the 2022 Uniform Transmission Rates. The way the Board can facilitate this is either to postpone the draft order process stage in this proceeding until after the 2022 cost of capital parameters are released, or simply require NextBridge to update the draft rate order again at that time. Waiting until the cost of capital parameters are released to finalize a utility revenue requirement is not uncommon, and often happens in the context of rate settlements, where the proposals are required to be filed before the Board had issued that year's cost of capital parameters.

***3.5.4*** ***Long and Short-Term Debt.*** NextBridge proposes to update the long-term and short-term debt rates based on what it secures in the financing it plans to undertake close to the March 31, 2022 effective date.[121] As SEC understands the proposal, the revenue requirement difference for 2022 and 2023 between the deemed amount included in rates and the actual rates will be recorded in the proposed Debt Rate Variance Account ("DRVA") to be cleared in the second annual update. It will then update the revenue requirement and, on a going forward basis for 2024 to reflect the actual debt rates.[122] NextBridge does not propose a similar update with respect to the ROE.

***3.5.5*** Even though it will make this update to its long-term debt, the base 2022 revenue requirement should still include the most up-to-date information. This ensures that any balance in the

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[119] Tr.1, p.39-40; OEB Staff IR Staff.67

[120] Filing Requirements For Electricity Transmission Applications, Chapter 2, Revenue Requirement Applications (February 11, 2016), p.33: "As per the 2009 Report, the OEB issues the cost of capital parameter updates for cost of service applications. Transmitters should use the most recent parameters as a placeholder, subject to an update if new parameters are available prior to the issuance of the OEB's decision for a specific transmitter's application."

[121] Tr.1, p.28-29,39,65-66

[122] H-1-1, p.5 (K1.2, p.13); Tr.3, p.129

DRVA and the update to the 2024 revenue requirement will be small and avoid intergenerational equity concerns.

*3.5.6* ***Return on Equity.*** Similar to long and short-term debt, SEC submits that NextBridge should be required to update the ROE to the most up-to-date numbers issued by the Board as required by the Filing Requirements. While the 2021 numbers are available, SEC submits, the better option is to wait until the 2022 cost of capital parameters are released in the fall to finalize the revenue requirement and the rate order.

*3.5.7* During the oral hearing, for the first time, NextBridge claimed that the reason it has not and does not propose to update cost of capital parameters is that Bamkushwada LP ("BLP") requires, for the purposes of applying for various government loan guarantee programs, that financial models it submits cannot change.[123] NextBridge has no actual knowledge of any such requirement, or even when these applications are required to be finalize and filed.[124] It was made very clear during the hearing that NextBridge is not actually involved in supporting those applications.[125] BLP has not made such a request to NextBridge in writing, nor has evidence of the requirements of these programs been filed in this proceeding. NextBridge also did not ask about BLP specifically about the impact of updating the ROE for the 2021 cost of capital parameters.[126]

*3.5.8* SEC submits NextBridge's rationale for wanting to "lock-in" the 2020 cost of capital parameters is not credible. When asked questions on updating its ROE during the interrogatory process, it never referred to this issue at all.[127] It is clear that the real reason it does not want to update the applications to incorporate the most recent cost of capital parameters is that the 2021 numbers are lower and would result in a reduction of the base revenue requirement by $2.5M.[128]

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[123] Tr.1, p.43; Tr.3, p.95-97

[124] Tr.3, p.96-98

[125] Tr.3, p.97

[126] Tr.3, p.96

[127] For example, see Interrogatory Response OEB Staff #66(a)

[128] Interrogatory Response OEB Staff #65

***3.5.9*** While it may be correct that BLP may not want to update certain models that it is required to file in applications with various government lending programs, it surely is not a requirement from those entities that the ROE amount be fixed by the OEB at this time. The Board's decision will have an impact on all aspects of the revenue requirement and rate plan. This includes the cost of debt, which NextBridge is proposing be updated through its proposed DRVA. Each of those will impact the very same models.

***3.5.10*** Furthermore, entities such as the Ontario Financial Authority, who manage the Aboriginal Loan Guarantee program[129], would be aware of the Board's annual process in updating the ROE using its well-known mechanistic formula.

### 3.6 ***<u>OM&A</u>***

***3.6.1*** NextBridge proposes a 2022 OM&A budget of $4.94M.[130] SEC submits that certain amounts related to certain compliance and administration costs appear higher than is reasonable. While SEC does not propose any specific reductions on this basis, it does provide evidence that the OM&A budget is far from "minimal" as claimed by NextBridge[131], and that it is sufficient to handle reasonable risks and cost pressures that may arise during the plan term.

***3.6.2*** SEC's area of concern is in the $1.67M of compliance and administration costs. A significant portion of these costs are covered by the NEET shared service agreement.[132] As discussed earlier, in contrast to what it claimed[133], it is clear NextBridge did not actually undertake a truly competitive process for the procurement of the services. At the hearing, Ms. Tidmash clarified that they did not send out an RFP for the non-operations and maintenance components of the OM&A work.[134] The evidence is that what it did do was simply ask each of its partners (i.e. NextEra, OMERS, and Enbridge) what their costs were to undertake these activities, and then determined it was NextEra based on the information it received.[135] SEC submits that this is not

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[129] Tr.3, p.97

[130] A-3-1, p.5 (K1.2, p.2); F-1-1

[131] Tr.1, p.68, 69, 90, 135, 138

[132] See Undertaking J3.4. ~63% ($1.045M/$1.670M) of the Compliance and Administration Costs are governed by the NEET Agreement.

[133] Interrogatory Response SEC #6 (K1.2, p.66)

[134] Tr.3, p.84

[135] Tr.3, p.85-86

appropriate.

***3.6.3*** If the NextBridge business model is that it will have no employees and outsource all of its work to third parties, it must ensure that the entity it chooses is the most cost effective option available. Simply asking its partners to provide their costs is not sufficient. It assumes that only those three entities can provide the service. This is obviously incorrect, considering Hydro One operates in the area, and was already chosen through a competitive process to do certain operation and maintenance work on the line in conjunction with SuperCom.

***3.6.4*** The approach taken by NextBridge is even more concerning when the entity contracted was that of a partner, and so the relationship is not arms-length. While SEC recognizes that NextEra is not technically an affiliate under the Board's Affiliate Relationship Code, as its ownership stake is not greater than 50%, it is still a related entity.[136] On that basis, it is especially concerning that the NEET agreement does not set out labour rates or any restrictions on those costs.[137] The NEET agreement simply provides that NextBridge will be responsible for all direct and indirect costs, defined as "pass-through costs", for work undertaken on its behalf.[138]

***3.6.5*** The OM&A benchmarking evidence undertaken by CRA, and filed by NextBridge, also raises flags regarding the reasonableness of the compliance and administration portion of the OM&A budget. The evidence is that NextBridge's administration and corporate cost category is more than 3 times the amount as the next highest amount.[139] While on a per kilometer basis, NextBridge's costs are more reasonable, unlike operation and maintenance costs, there should not be a linear relationship between length of the line and corporate and administrative costs.[140]

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[136] Interrogatory Response OEB Staff #28(b)

[137] Tr.3, p.85-86

[138] Undertaking J3.5

[139] B-1-7, p.17

[140] B-1-7, p.17

# 4 OTHER ISSUES

## 4.1 *Deferral and Variance Accounts*

*4.1.1* ***Capital Construction Variance Account.*** See section 3.3.

*4.1.2* ***Debt Rate Variance Account.*** See section 3.5.

*4.1.3* ***Revenue Deferral Variance Account.*** NextBridge has proposed a variance account to true-up the revenue requirement difference between the forecast March 31, 2021 effective date and the actual in-service date, is reasonable.[141] SEC submits that this account is appropriate, but it is important to emphasize the comments made by NextBridge at the oral hearing, that until it has actually been successfully tested with electricity flowing through it, the line is not in-service.[142] This is the case even if NextBridge has completed construction, but Hydro One has been delayed in constructing the required transmission stations for the line to be operational.[143]

*4.1.4* ***Taxes or Payments in Lieu of Taxes Variance Account ("PILsVA").*** NextBridge's proposed account mirrors the Board's generic Account 1592, with one addition. The proposed account would not only track the revenue requirement impact of legislative or regulatory changes of tax rates and rules, but also those resulting from the expect BLP buy-in and any subsequent changes in its tax-exempt status.[144] SEC does not have an issue with the proposed account, on the condition that the Board's long-standing practice that there is a 50/50 sharing of any balances (credit or debit) in Account 1592 is applied to any balance in this account.[145]

## 4.2 *Costs*

*4.2.1* SEC hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that SEC has participated responsibly in all aspects of the process, in a manner designed to assist the Board as efficiently as possible.

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[141] Tr.1, p.56; H-1-1, p.2 (K1.2, p.10)

[142] Tr.1, p.57-58

[143] Tr.1, p.57-58

[144] H-1-1, p.1 (K1.2, p.9)

[145] See Filing Requirements For Electricity Distribution Rate Applications - 2020 Edition for 2021 Rate Applications - Chapter 2, p.37

ALL OF WHICH IS RESPECFULLY SUBMITTED.

Mark
Rubenstein
2021-04-27
15:41:36

Mark Rubenstein
Counsel for the School Energy Coalition

# A

| 1 | **SEC Analysis (Cost of Service vs. NB RCI Proposal)** | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2 | | **2022** | **2023** | **2024** | **2025** | **2026** | **2027** | **2028** | **2029** | **2030** | **2031** | **TOTAL** |
| 3 | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | |
| 4 | **Capital Related RR** | | | | | | | | | | | |
| 5 | Rate Base ($M) | 770.4 | 763.9 | 755.3 | 746.7 | 737.9 | 728.8 | 719.8 | 711.1 | 702.4 | 693.3 | |
| 6 | | | | | | | | | | | | |
| 7 | Cost of LT Debt ($M) (1) | 13.85 | 13.73 | 13.58 | 13.42 | 13.26 | 13.10 | 12.94 | 12.78 | 12.63 | 12.46 | |
| 8 | Cost of ST Debt ($M) (1) | 0.85 | 0.84 | 0.83 | 0.82 | 0.81 | 0.80 | 0.79 | 0.78 | 0.77 | 0.76 | |
| 9 | Return on Equity ($M) (1) | 26.26 | 26.03 | 25.74 | 25.45 | 25.15 | 24.84 | 24.53 | 24.24 | 23.94 | 23.63 | |
| 10 | | | | | | | | | | | | |
| 11 | *Total Cost of Capital* ($M) | 41.0 | 40.6 | 40.1 | 39.7 | 39.2 | 38.7 | 38.3 | 37.8 | 37.3 | 36.9 | |
| 12 | | | | | | | | | | | | |
| 13 | Depreciation ($M) | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | 9.3 | |
| 14 | Income Taxes ($M) | 0.6 | 0.6 | 0.6 | 0.6 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | |
| 15 | | | | | | | | | | | | |
| 16 | **Total Capital RR ($M)** | 50.8 | 50.4 | 50.0 | 49.5 | 49.0 | 48.6 | 48.1 | 47.6 | 47.2 | 46.7 | |
| 17 | | | | | | | | | | | | |
| 18 | **OM&A** | | | | | | | | | | | |
| 19 | OM&A ($M) (2) | 4.9 | 5.0 | 5.1 | 5.2 | 5.3 | 5.5 | 5.6 | 5.7 | 5.8 | 5.9 | |
| 20 | | | | | | | | | | | | |
| 21 | ***Total Annualized RR ($M)*** | 55.7 | 55.5 | 55.1 | 54.8 | 54.4 | 54.0 | 53.7 | 53.3 | 53.0 | 52.6 | **542.0** |
| 22 | | | | | | | | | | | | |
| 23 | ***April 1, 2022 Effective Date RR ($M) (3)*** | 41.8 | 55.5 | 55.1 | 54.8 | 54.4 | 54.0 | 53.7 | 53.3 | 53.0 | 52.6 | **528.1** |
| 24 | | | | | | | | | | | | |
| 25 | ***NB Proposal Annualized RR ($M)*** | 55.7 | 56.8 | 58.0 | 59.1 | 60.3 | 61.5 | 62.8 | 64.0 | 65.3 | 66.6 | **610.1** |
| 26 | | | | | | | | | | | | |
| 27 | ***NB Proposal April 1, 2022 Effective Date ($M) (3*** | 41.8 | 56.8 | 58.0 | 59.1 | 60.3 | 61.5 | 62.8 | 64.0 | 65.3 | 66.6 | **596.2** |
| 28 | | | | | | | | | | | | |
| 29 | (1) Cost of capital parameters fixed for term. Numbers from application. | | | | | | | | | | | |
| 30 | (2) Assumed annual OM&A increase of 2% to match NB inflation number | | | | | | | | | | | |
| 31 | (3) Assumed April 1, 2022 effective date as proposed by NB, 2022 RR included at 9/12th of year | | | | | | | | | | | v.2 |

# B

| 1 | | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | Notes |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2 | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | |
| 3 | | | | | | | | | | | | |
| 4 | **Rate Base** | | | | | | | | | | | |
| 5 | ***Base 2022 Rate Base*** | | | | | | | | | | | |
| 6 | Opening Gross Book Value | 774.94 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 2022 data from Appendix 2-BA (C-4-1, Attach 3, p.2) |
| 7 | Additions Gross Book Value | 0.23 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| 8 | Closing Gross Book Value | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | 775.17 | |
| 9 | Opening Acc Dep | 0.00 | 6.95 | 16.21 | 25.47 | 34.73 | 43.99 | 53.25 | 62.51 | 71.77 | 81.03 | Adjusted 2023 for prorated year of service in 2022 (NB Correction) |
| 10 | Additions to Acc Dep | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | 9.26 | |
| 11 | Closing Acc Dep | 9.26 | 16.21 | 25.47 | 34.73 | 43.99 | 53.25 | 62.51 | 71.77 | 81.03 | 90.29 | |
| 12 | Avg NBV | 770.43 | 763.60 | 754.34 | 745.08 | 735.82 | 726.56 | 717.30 | 708.04 | 698.78 | 689.52 | |
| 13 | | | | | | | | | | | | |
| 14 | ***Additional TSP Expenditures*** | | | | | | | | | | | |
| 15 | Closing Gross Book Value | 0 | 0.59 | 1.33 | 1.97 | 2.25 | 2.45 | 2.86 | 3.65 | 3.95 | 4.05 | 2023-2031 data from IR Staff.34(b) |
| 16 | Closing Acc Dep | 0 | 0.01 | 0.02 | 0.05 | 0.07 | 0.1 | 0.14 | 0.18 | 0.23 | 0.28 | |
| 17 | Closing NBV | 0 | 0.58 | 1.31 | 1.92 | 2.18 | 2.35 | 2.72 | 3.47 | 3.72 | 3.77 | |
| 18 | Avg NBV | 0 | 0.29 | 0.95 | 1.62 | 2.05 | 2.27 | 2.54 | 3.10 | 3.60 | 3.75 | |
| 19 | | | | | | | | | | | | |
| 20 | Total Avg NBV | 770.43 | 763.89 | 755.28 | 746.69 | 737.87 | 728.82 | 719.83 | 711.13 | 702.37 | 693.26 | Row 12+18 |
| 21 | | | | | | | | | | | | |
| 22 | ***Cost of Capital*** | | | | | | | | | | | |
| 23 | LTD (1) | 13.85 | 13.73 | 13.58 | 13.42 | 13.26 | 13.10 | 12.94 | 12.78 | 12.63 | 12.46 | Cost of capital paramaters G1-1-1, p.3 |
| 24 | STD (1) | 0.85 | 0.84 | 0.83 | 0.82 | 0.81 | 0.80 | 0.79 | 0.78 | 0.77 | 0.76 | |
| 25 | ROE (1) | 26.26 | 26.03 | 25.74 | 25.45 | 25.15 | 24.84 | 24.53 | 24.24 | 23.94 | 23.63 | |
| 26 | | | | | | | | | | | | |
| 27 | Total Cost of Capial | 40.95 | 40.61 | 40.15 | 39.69 | 39.22 | 38.74 | 38.26 | 37.80 | 37.34 | 36.85 | Row 23+24+25 |
| 28 | | | | | | | | | | | | |
| 29 | **OM&A & Depreciation** | | | | | | | | | | | |
| 30 | ***Depreciation*** | 9.26 | 9.27 | 9.27 | 9.29 | 9.28 | 9.29 | 9.30 | 9.30 | 9.31 | 9.31 | F-11-1, p.2 + Difference in y/y Acc Dep (Row 16) |
| 31 | | | | | | | | | | | | |
| 32 | ***OM&A (2)*** | 4.94 | 5.04 | 5.14 | 5.24 | 5.35 | 5.45 | 5.56 | 5.67 | 5.79 | 5.90 | F-4-1, p.2 (2022) |
| 33 | | | | | | | | | | | | |
| 34 | **Income Taxes** | | | | | | | | | | | |
| 35 | Reg Net Income/Return of Equity | 26.26 | 26.03 | 25.74 | 25.45 | 25.15 | 24.84 | 24.53 | 24.24 | 23.94 | 23.63 | |
| 36 | Add back depreciation | 9.26 | 9.27 | 9.27 | 9.29 | 9.28 | 9.29 | 9.30 | 9.30 | 9.31 | 9.31 | |
| 37 | CCA | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | -30.5 | CCA for 2022 base assets only. Have not included CCA for 2023-2031 additions which are not known. |
| 38 | CCA (AII) | -60.9 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | |
| 39 | *Taxable Income* | -55.9 | 4.8 | 4.5 | 4.2 | 3.9 | 3.6 | 3.3 | 3.0 | 2.7 | 2.4 | |
| 40 | Loss Carryforward | 0 | -55.9 | -51.1 | -46.6 | -42.3 | -38.4 | -34.8 | -31.4 | -28.4 | -25.7 | |
| 41 | *Revised Taxable Income* | -55.9 | -51.1 | -46.6 | -42.3 | -38.4 | -34.8 | -31.4 | -28.4 | -25.7 | -23.2 | |
| 42 | | | | | | | | | | | | |
| 43 | Tax Rate | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | 26.5% | |
| 44 | Tax/PILs | -14.81 | -13.54 | -12.34 | -11.22 | -10.18 | -9.22 | -8.33 | -7.53 | -6.80 | -6.16 | |
| 45 | *Grossed Up Income Taxes* | -20.15 | -18.42 | -16.79 | -15.26 | -13.85 | -12.54 | -11.34 | -10.24 | -9.25 | -8.37 | |
| 46 | | | | | | | | | | | | |
| 47 | Accounting Income | 21.03 | 20.85 | 20.62 | 20.38 | 20.14 | 19.90 | 19.65 | 19.41 | 19.17 | 18.92 | Row 35 * (1-0.199) |
| 48 | OCMT Rate | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | 2.70% | |
| 49 | *OCMT* | 0.6 | 0.6 | 0.6 | 0.6 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | Row 47 * 2.7% |
| 50 | | | | | | | | | | | | |
| 51 | ***Total Income Taxes Payable*** | 0.6 | 0.6 | 0.6 | 0.6 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | OCMT applied if no taxable income |
| 52 | | | | | | | | | | | | |
| 53 | **Total Annualized RR** | **55.72** | **55.48** | **55.11** | **54.77** | **54.39** | **54.02** | **53.66** | **53.30** | **52.95** | **52.58** | Row 27+30+30+32+51 |
| 54 | | | | | | | | | | | | |

| 55 | | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2022-2026 (3) | 2027-2031 | 2022-2031 (3) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 56 | **Forecast RR** | 55.72 | 55.48 | 55.11 | 54.77 | 54.39 | 54.02 | 53.66 | 53.30 | 52.95 | 52.58 | 261.55 | 266.51 | 528.05 |
| 57 | **Nextbridge Proposal (4)** | 55.72 | 56.83 | 57.97 | 59.13 | 60.31 | 61.52 | 62.75 | 64.01 | 65.29 | 66.59 | 276.04 | 320.15 | 596.19 |
| 58 | | | | | | | | | | | | | | |
| 59 | **Forecast ROE** | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% | 8.52% |
| 60 | **Nextbridge Proposal ROE** | 8.52% | 8.96% | 9.47% | 9.98% | 10.53% | 11.09% | 11.68% | 12.28% | 12.91% | 13.57% | 9.49% | 12.31% | 10.90% |

(1) Cost of capital parameters fixed for term. Numbers from application.

(2) Assumed annual OM&A increase of 2% to match NB inflation number.

(3) Assumed April 1, 2022 effective date as proposed by NB, 2022 RR included at 9/12th of year

(4) Exhibit E1-1-1, p.2

v.2

# C

| ***Capital Adjustment Factor*** | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Capital-Related RR ($M)** | 50.78 | 50.44 | 49.97 | 49.53 | 49.05 | 48.57 | 48.09 | 47.62 | 47.16 | 46.67 |
| **Annual Reduction (%)** | | -0.67% | -0.92% | -0.89% | -0.98% | -0.97% | -0.98% | -0.97% | -0.97% | -1.04% |
| **Average** | | | | | | | | | | -0.93% |

| ***SEC Proposal*** | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2022-2026* | 2027-2031 | 2022-2031* | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Split RR (Capital RR - Cap Adj Factor) OM&A (I-X)** | | | | | | | | | | | | | | | |
| **Capital-Related RR ($M)** | 50.78 | 50.32 | 49.87 | 49.42 | 48.98 | 48.54 | 48.10 | 47.67 | 47.24 | 46.81 | | | | **Capital Adj Factor** | 0.90% |
| **OM&A ($M)** | 4.94 | 5.02 | 5.11 | 5.20 | 5.28 | 5.37 | 5.47 | 5.56 | 5.65 | 5.75 | | | | **I-Factor** | 2.00% |
| **Total RR ($M)** | ***55.72*** | ***55.35*** | ***54.98*** | ***54.62*** | ***54.26*** | ***53.91*** | ***53.57*** | ***53.23*** | ***52.89*** | ***52.56*** | 261.00 | 266.15 | 527.15 | **X-Factor** | 0.30% |
| **ROE (%)** | 8.52% | 8.48% | 8.49% | 8.48% | 8.50% | 8.51% | 8.52% | 8.53% | 8.55% | 8.57% | 8.49% | 8.54% | 8.52% | | |

* Assumed April 1, 2022 effective date as proposed by NB, 2022 RR included at 9/12th of year

| ***Alternative Appraoch*** | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2022-2026* | 2027-2031 | 2022-2031* | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Total RR (I-X-Adj Factor)** | | | | | | | | | | | | | | | |
| ***Total RR*** | ***55.72*** | ***55.36*** | ***55.00*** | ***54.64*** | ***54.29*** | ***53.93*** | ***53.58*** | ***53.23*** | ***52.89*** | ***52.54*** | 261.07 | 266.18 | 527.26 | **Adj Factor** | 2.35% |
| ***ROE*** | 8.52% | 8.49% | 8.49% | 8.49% | 8.50% | 8.52% | 8.53% | 8.54% | 8.55% | 8.56% | 8.50% | 8.54% | 8.52% | **I-Factor** | 2.00% |
| | | | | | | | | | | | | | | **X-Factor** | 0.30% |

* Assumed April 1, 2022 effective date as proposed by NB, 2022 RR included at 9/12th of year