

October 15, 2021

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

Dear Ms. Long

Re: **EB-2021-0212**
OEB Review of Inflation Factor for 2022 IRM rate setting

Thank you for the opportunity to reply to parties' October 1 comments in the above-named matter.

These are the reply comments of the Electricity Distributors Association (EDA). These comments are premised on our members' position that, first and foremost, the OEB needs to provide sound, principled economic regulation. We propose that the OEB reject parties' comments supporting replacing the Average Weekly Earnings (AWE) with another factor:

- parties have not provided evidence that the AWE is unsuitable for rate making purposes
- parties have not shown that rates based on the AWE cannot be authorized as just and reasonable
- parties have not demonstrated that the estimated bill impact of 0.6% (or 20 basis points higher than the other Option whose bill impact was modelled) is so high as to warrant revisions to the OEB's long standing Incentive Rate-setting Mechanism (IRM) policy.

Data Issues

The EDA proposes that the OEB use the AWE for rate setting purposes in 2022 as no party has provided either evidence or analysis demonstrating the inappropriateness of using the AWE.

Several parties commented that the OEB should suspend the use of the AWE, typically on the grounds that it inappropriately reflects the effects of changes to work force composition rather than changes in labour cost rates. Parties did not provide evidence or analysis to support their comments on the inappropriateness of using the AWE. The EDA's October 1 comments discussed that our members are subject to work force composition risks (e.g., through their contractors' experiences in the labour market). We also note that parties have not tested their tacit assumption that the AWE's pre-COVID composition aligns appropriately with the composition of LDCs' workforces. Our October 1 comments provided links to articles on inflation forecasts; they show that the observed change in the rate of inflation is in the 3% - 3.5% range – and is consistent with the Inflation Factor computed using the AWE.

No party provided an analysis of the pandemic's impact on the labour market, on wages or refuted the analysis provided in OEB staff's Fact Sheet of the AWE (e.g., whether the compositional and/or inflationary effects impacting the AWE are transitional, will be short lived, will be long lived or will endure). This is the first instance of the OEB engaging in the AWE's sensitivity to compositional issues. The OEB cannot act on parties' doubts of the appropriateness of the AWE for rate making purposes that arise from the manifestation of that sensitivity. Doubts that are not supported by evidence or analysis are not a reason to abandon a principle driven framework for setting rates. Doubts are not a principled reason to reject a regulatory policy.

Some parties suggest that the OEB should replace the AWE and many parties demonstrated the expected rate impacts that customers could experience if their alternative data set were adopted. These parties did not provide evidence or any other analysis in support of their position. The parties who advocate that the GDP IPI FDD be used instead of the AWE are, in simple terms, advocating for a return to a past practice that the OEB deliberately set aside in 2013. Among the OEB's reasons, as set out in the Report of the Board (EB-2010-0379), for adopting the current two factor inflation metric was that it provides an Ontario specific inflation factor that better indicates Ontario input price fluctuations and it provides a component to adjust for labour prices. No party has demonstrated that these reasons should be set aside.

A party advocated for blending data from two different time periods – without providing analysis or evidence in support of this position, other than to quantify the impact to rates. We note that the OEB's Report of the Board (EB-2010-0379) discussed and ultimately rejected using a three-year moving average to quantify the inflation factor. That report discussed the OEB's concern that a moving average embeds extreme values of inflation for the duration of the period of the rolling average. That concern will be manifested in the proposed blending of data from different time periods and we propose that the OEB reject this proposal, for the same reasons that it rejected the proposal to use a moving average.

A party noted that AWE sub-indices exhibit markedly different outcomes. We urge the OEB not to adopt this position: it risks 'cherry picking' indices for the purposes of setting rates for 2022 and, if the utilities sub-index is relied on, it risks data circularity (i.e., that LDCs' changes in costs in one period will be used to set rates in a future period and influence LDCs' level of costs) issues in future periods. We note that while some parties expressed that the OEB needs to be prepared to rely on its choice of inflation factor for two or more years, none of them considered the possibility that their proposed data set could result in an unusual change in a future period.

Inflation Factor issues

No party has shown that it is inappropriate to use the AWE for rate setting purposes in 2022 on the grounds that it will or may result in an inappropriate inflation factor.

OEB staff recognized that:

- regulatory policies should be followed, unless there is a good reason not to, to achieve predictability, consistency, and efficiency
- the estimated total bill impact for customers arising from their Option 3 index is 0.2% greater than the estimated bill impact of their Option 1.

The EDA comments that a bill change of this magnitude is not a sufficient reason to alter a component of the IRM thereby risking compromising regulatory consistency, predictability and understandability. The EDA points out that School Energy Coalition made a related comment that the OEB needs to understand how the decision it makes in this proceeding will impact future calculated Inflation Factors, and whether it risks distortions in the future.

Rate making issues

The evidence and analysis on the record is insufficient to support deviating from regulatory policy chiefly because of its impact on regulatory certainty, predictability and understandability versus the estimated modest bill impact of 0.6%.

As our October 1 comments discussed, the OEB's duty is to authorize just and reasonable rates and to achieve their legislative objectives, including the objective to maintain a financially viable sector. Whether the OEB is setting rates using the Cost of Service Methodology or the IRM it is to authorize rates that are just and reasonable that:

- recover the ongoing costs incurred to provide service
- provide the LDC with the opportunity to earn the allowed rate of return
- are free of undue cross subsidization.

Several parties advocated for the AWE to be 'over written' or 'replaced' by a data series that, from their perspective, is more suitable for rate making purposes. None of these parties addressed the appropriateness of altering one element of the IRM Framework in isolation, despite the framework being a coordinated package. Those parties typically supported their recommended data set with a calculation of how it impacts rates – with a focus on how it achieves rate stability. They did not address how their proposed data set results in rates that can be authorized as just and reasonable.

Some parties implied that stability level or quantum of rates between periods is a criterion of just and reasonable rates. This is not a feature of just and reasonable rates, rather it is an implementation issue that arises from time to time depending on the level of rate or bill change that customers can be expected to experience. Good rate making uses data and a specific methodology to quantify rates and the regulator subsequently addresses how to best implement the resulting rates (e.g., to address perceived rate shock or bill shock, neither of which is expected to occur under any of the options identified in OEB staff's Fact Sheet). The OEB has rate making tools that it can use to smooth rate changes (e.g., using a Foregone Revenue Deferral Account). The EDA's position that the predictability, stability and understandability of the rate setting methodology is an aspect of a sound rate setting regime is correct. The OEB cannot adopt parties' implicit assertion that the stability of the rate setting

regime methodology is proxied or demonstrated by the stability of the quantum of the resulting rates.

LDCs bill their customers for distribution service using OEB authorized just and reasonable rates. The attributes of just and reasonable rates are set out on page 3. From a principled perspective, parties' assertion that the OEB should, when setting just and reasonable rates, pay heed to the affordability of the authorized rates and consider the consumer's ability to pay the resulting bill is not correct. We note that OEB staff's Fact Sheet shows that Option 1 results in an estimated bill impact of 0.6%. We must point out that if bill impacts were material government has provided funding mechanisms (e.g., COVID Emergency Assistance Program) and policies (e.g., pandemic Regulated Price Plan rates) geared to supporting customers' ability to pay their electricity bills while pandemic conditions persist.

London Property Managers Association (LPMA) proposed that the OEB could adopt Option 1 and achieve a level of fairness if each LDC credited its COVID Deferral Account with an amount equal to the revenue impact of the difference between:

- Option 1's estimated rate change
- the inflation factor that would result from the use of the 2019 AWE

LPMA provided neither evidence nor analysis demonstrating how this approach results in an appropriate level of fairness. This position appears to inappropriately mix the purpose of the COVID deferral account with good rate making that sets base distribution rates prospectively. The proposal conflicts with the OEB's design of the COVID Deferral Account: the OEB established the COVID Deferral Account to capture the financial effects of the pandemic, not the rate making effects of different labour inflators, and the OEB explicitly precluded recording lost revenues in the account. Among the implementation issues that were not addressed are:

- whether the OEB's means test for the COVID Deferral Account will result in a range of Inflation Factors, and the appropriateness of deviating from the OEB's policy of providing a universal Inflation Factor
- whether the OEB should proceed generically when disposing of this component of the COVID deferral account or should provide it to those LDCs that file an application seeking disposition of the balance record in their COVID deferral account
- whether to dispose of the portion of the account's balance related to the rate change differential through a rate adder that would operate until the LDC next rebases or through a rate rider that would achieve a one-time disposition
- the appropriate rate making treatment if a portion of the difference was correctly attributable to inflation.

This proposal appears to push the decision of the appropriate rate change to a future date when the LDC seeks disposition of the balance recorded in its COVID Deferral Account – and was offered without foresight of how it could impact either LDCs or their customers now or in future periods. Like many other comments made by parties, this party did not address how its proposal results in rates that can be authorized as just and reasonable. For these reasons we propose that the OEB reject this position.

The IRM results in rates that are cost related. Some parties have commented that the OEB should adopt a different data set as a proxy for labour cost changes because it will align better with the cost pressures that LDCs can be expected to experience. They have provided neither evidence nor analysis to support the need to improve this alignment, nor of the appropriateness of improving any alignment through a rate making mechanism that is designed to yield cost related rates.

Process issues

The EDA makes no reply comments on process issues.

What to do next?

The EDA supports the OEB in continuing to use the AWE, OEB staff's Option 1, to quantify rates set pursuant to the IRM in 2022. We caution that positions not supported by evidence, due diligence, analysis or foresight should be regarded as speculative and given little weight.

Thank you again for the opportunity to comment. If you have any questions on these comments or require any clarification, please do not hesitate to contact Kathi Farmer, the EDA's Senior Regulatory Affairs Advisor at kfarmer@eda-on.ca or at 416.659.1546.

Sincerely,

A handwritten signature in black ink, appearing to read 'Teresa Sarkesian', written in a cursive style.

Teresa Sarkesian
President and Chief Executive Officer