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March 4, 2022

Delivered by Email & RESS

Ms. Marconi, Acting Registrar
Ontario Energy Board
P.O. Box 2319, 27th Floor
2300 Yonge Street
Toronto, ON M4P 1E4

Dear Ms. Marconi:

Re: North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation
Ontario Energy Board File No.: EB-2021-0312
MAADs Application under Section 86 of the *Ontario Energy Board Act, 1998* and Related Relief

We are counsel to the Applicants in the above-noted proceeding (the "Proceeding"). Please find enclosed the reply submissions of North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation.

If you have any questions or concerns, please do not hesitate to contact me.

Yours very truly,

BORDEN LADNER GERVAIS LLP

Per:

J Vellone

John Vellone
cc: Melissa Casson, Vice President of Finance, NBHDL
Matt Payne, President and Chief Executive Officer, NBHDL

EB-2021-0312

IN THE MATTER OF Sections 86 and 18 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sched. B, as amended;

AND IN THE MATTER OF an application for leave to amalgamate North Bay Hydro Distribution Limited ("**NBHDL**") and Espanola Regional Hydro Distribution Corporation ("**ERHDC**") into an entity referred to in this Application as "New NBHDL", made pursuant to section 86(1)(c) of the Ontario Energy Board Act, 1998 and other relief as described under Section 2 of this application.

REPLY SUBMISSIONS OF
THE APPLICANTS (NBHDL & ERHDC)

MARCH 4, 2022

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1. We are counsel to North Bay Hydro Distribution Limited ("**NBHDL**") and Espanola Regional Hydro Distribution Corporation ("**ERHDC**", and collectively, the "**Applicants**") in respect of the application filed November 24, 2021 under Section 86(1)(c) of the *Ontario Energy Board Act, 1998* for approval to amalgamate and continue operations as a new single local distribution company called North Bay Hydro Distribution Limited ("**New NBHDL**") and related relief as more specifically set out in Section 2 of the application (the "**Application**").

2. We are pleased to present the following reply to the submissions made in respect of the Application received from OEB Staff on February 25, 2022 (the "**OEB Staff Submissions**"), School Energy Coalition on February 25, 2022 (the "**SEC Submissions**"), and from Donald D. Rennick on February 26, 2022 (the "**DDR Submissions**").

A. THE "NO HARM" TEST

3. Both OEB Staff[1] and SEC[2] agree that the proposed transaction satisfies the no harm test. In respect of price, economic efficiency and cost effectiveness both OEB Staff[3] and SEC[4] take note in their submissions of the forecasted OM&A synergies, which start at $657k in 2023 and increase to $686k in 2027,[5] arising in part from the termination of the PUC Services Agreement without the need for New NBHDL to increase its FTE levels in response to the incremental responsibilities.[6] Both OEB Staff[7] and SEC[8] acknowledge that ratepayers of both ERHDC and NBHDL stand to <u>benefit</u> from the proposed transaction, as evidenced by the forecasted reduction in OM&A per customer found at Table 1-6 of the Application.

4. The Applicants agree.

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[1] OEB Staff Submissions at page 2.
[2] SEC Submissions at page 3.
[3] OEB Staff Submissions at page 4.
[4] SEC Submissions at pages 2-3.
[5] Application at Table 6-1.
[6] SEC-8.
[7] OEB Staff Submissions at page 3.
[8] SEC Submissions at page 3.

5. OEB Staff[9] further note that the forecasted transaction costs and transition costs will not be recovered from ratepayers, but rather will be funded through residual earnings.[10] In respect of reliability and quality of service, both SEC[11] and OEB Staff[12] take note of New NBHDL's plan to maintain ERHDC's operations centre in its current location to continue to provide local service to customers in the ERHDC service territory. OEB Staff[13] further notes further potential for reliability improvements if NBHDL is able to extend its SCADA system to the ERHDC service territory. Finally, in respect of financial viability, OEB Staff notes that the proposed amalgamation will have no adverse impacts on the financial viability of either utility.

6. The Applicants again agree.

B. THE SUBMISSIONS OF MR. RENNICK

7. In this context, Mr. Rennick argues that the proposed transaction fails to satisfy the no harm test for three reasons:

i. Mr. Rennick believes that NBHDL customers will need to fund debt payments of over $5 million over the next 25 years;
ii. Mr. Rennick believes the combined debt/equity ratio will be 1.46 which in his view is detrimental to future borrowing; and
iii. Mr. Rennick does not believe the forecasted synergies, because NBHDL management sought several incremental FTEs in the EB-2020-0043 rate case.

8. The Applicants do not agree. We will reply to each of these three reasons in-turn below.

i. NBHDL customers will not need to fund ERHDC debt

9. Mr. Rennick argues that the Applicants failed to respond appropriately to DDR-1 and that if the Applicants had responded appropriately there would be a cash shortage of $5.1 million

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[9] OEB Staff Submissions at page 3.
[10] Application at Section 7.2.
[11] SEC Submissions at page 3.
[12] OEB Staff Submissions at page 4.
[13] OEB Staff Submissions at page 4 citing SEC-6 and 1-Staff-1(b).

funded through ERHDC rates.[14]

10. The Applicants do not agree. The question was answered in a fulsome and appropriate manner with specific reference to the pro-forma financial statements and scorecard that was filed with the Application and also with specific reference to the factors that are relevant to the OEB in making a determination on the no harm test (i.e. financial viability).

11. The evidence is clear that the cost of capital component of ERHDC revenue requirement is more than enough to fund the interest payments on this debt.

12. In submissions, Mr. Rennick then makes an implausible and unrealistic assumption that the Applicants would seek to pay down 100% the ERHDC long-term debt over a 25 year period rather than refinancing those loans from time-to-time as would normally be the case (thus maintaining the prescribed debt-to-equity ratio over time).

13. If one assumes that 100% of the principal on long-term debt is to be repaid in 25 years, then one must also assume that ERHDC is no longer a going concern in 25 years. You cannot run a capital intensive business like an electricity distributor without capital. This is why this is an implausible and unrealistic assumption.

14. When modelling this unrealistic scenario,[15] which modelling is untested, error filled and which the OEB should give no weight to, Mr. Rennick errs by comparing the *nominal* cash outlays on the loans over 25 years ($11.3m) with *real* cash inflows ($387k * 25) without accounting for the time value of money on the cash inflows. If one assumes a 2% rate of inflation on the cash inflows (which is reasonable given recent OEB IRM escalation factors), the comparison results in a $1.2m surplus not a shortfall.

15. In addition, Mr. Rennick fails to account for annual depreciation of $226,618 generated through ERHDC rates.[16] If one assumes ERHDC would no longer be a going concern in 25 years, then this depreciation would be available to fund the principal repayments resulting

[14] DDR Submissions at pages 1 and 2.
[15] See "DDR – IRR Submissions re Loan Payment Cash flow_.xls"
[16] See the Decision and Rate Order dated June 10, 2021 in EB-2020-0020 at Schedule B, Table A, found at Page 10 of 65 of the OEB approved settlement proposal.

in a surplus of cash using Mr. Rennick's modelling, not a cash deficiency as alleged by Mr. Rennick.

16. In any event, none of this is relevant to the proposed transaction that is the subject of this Application. To the extent Mr. Rennick is objecting to the acquisition debt used to finance the Phase 1 transaction, that matter was fully addressed by the OEB in its approval of the Phase 1 transaction in its Decision and Order dated August 22, 2019 (EB-2019-0015).[17]

17. No new debt is being assumed in connection with the proposed amalgamation that is the subject of this Application and no purchase price is being paid.

18. In addition, as explained in Section 7.4 of the Application, ERHDC currently relies heavily on NBHDL guarantees to support external financing requirements. The proposed transaction will eliminate the need for these guarantee arrangements, significantly improving the financial viability of ERHDC without negatively impacting the financial viability of New NBHDL.

ii. The proposed transaction will not negatively impact New NBHDL's financial viability or borrowing capacity

19. As is shown in response to DDR-1, New NBHDL's total debt to equity ratio is forecasted to be 1.29 in 2023 – which remains well below the OEB's target of 1.5.

20. In this context, Mr. Rennick calculates something he refers to as a "debt to equity ratio" of 1.46 to suggest that this puts the future borrowing capacity of New NBHDL at risk.

21. This is simply not true.

22. The Applicants do not agree with Mr. Rennick's calculation. He arbitrarily deducts \$3,350,696[18] of goodwill from total equity even though goodwill is included as an intangible asset on the balance sheet (not part of shareholder's equity). The goodwill included in the

[17] Mr. Rennick made similar submissions in objection to the Phase 1 transaction – including filing the "DDR_Purchase Price_Loan Amortization Schedule.xls".
[18] The Applicants do not know where Mr. Rennick gets this number from, given that the pro-forma financial statements provide a goodwill amount of \$3,322,007.

pro-forma has been the subject of an annual impairment test as part of audits conducted in 2019, 2020 and 2021 – and it has not been impaired – and the Applicants believe that it will not be impaired given the expected synergies arising from the proposed amalgamation.

23. He also arbitrarily increases the debt values by a mark-to-market valuation, which is not typical in calculation of a debt to equity ratio. The mark-to-market value would only be relevant to this type of calculation if the Applicants unwound the related SWAPs which is not an action the Applicants would take.

24. While NBHDL follows the OEB calculation of the debt to equity ratio used in the scorecard, Mr. Rennick has invented his own methodology to arrive at numbers that better suits his arguments. Mr. Rennick's approach is not appropriate.

25. As explained in Section 7.4 of the Application, New NBHDL will continue to have strong liquidity and debt service ratios as well as a more optimal debt to equity ratios with sufficient financial capacity for necessary borrowing.

iii. The forecasted synergies are clearly evidenced and entirely unrelated to incremental FTEs sought in the EB-2020-0043 rate case

26. This case is relatively simple given that most of the synergies arise due to the expiry of a single contract - the PUC Services Agreement,[19] a copy of which was attached as Appendix "A" to the IRRs. Additional synergies will arise from the amalgamation itself arising from elimination in duplication in both businesses, which savings were more fully detailed in response to SEC-4.

27. In response to SEC-3, the Applicants further confirmed that NBHDL will not be increasing its FTEs in order to undertake the incremental responsibilities of assuming functions under the PUC Services Agreement.

28. Mr. Rennick clearly disagrees with this fact.

[19] Application at page 15.

29. However, the new FTEs that were ultimately approved by the OEB in the EB-2020-0043 Decision and Order (as well as the proposed FTEs that were not approved) were all the subject of discovery and argument in that other proceeding and are not relevant to the matters at issue in this application.

30. It is noteworthy that the evidence in EB-2020-0043 was that those FTEs were needed regardless of whether the proposed amalgamation at issue in this case proceeded or not. Specifically, the evidence filed in EB-2020-0043 included business cases supporting each proposed FTE. None of those business cases suggested that those FTEs were required due to an amalgamation that, at the time, had not yet occurred. Rather the FTEs were required to meet specific business needs of NBHDL regardless of whether or not the amalgamation with ERHDC occurs.

31. In any event, this application is not an appropriate forum to engage in a rehashing of the evidence filed and arguments that were made in EB-2020-0043.

32. Nothing cited by Mr. Rennick supports his casual dismissal of the fact outlined in the response to SEC-3. No new FTEs will be hired to undertake the incremental responsibilities associated with assuming the functions under the PUC Services Agreement.

C. OTHER MATTERS

33. OEB Staff submit that the Applicants have addressed, either in this Application or in prior applications, all directions and orders from previous OEB decisions that are pertinent to this Application.[20]

34. The Applicants agree. The Applicants carefully set out all prior directions and orders relevant to this application in Section 1.2 of the Application and ensured that each was either satisfied in a prior application or was addressed in the evidence in this Application.

35. OEB Staff also submit that the proposed services agreement between ERHDC and NBHDL

[20] OEB Staff Submissions at pg. 6.

for the period until the entities merge, is appropriate and compliance with OEB policies.

36. The Applicants again agree. A copy of an ARC compliant services agreement between ERHDC and NBHDL has been filed as Appendix B of the IRRs.

37. With regards to the ESM, OEB Staff correctly observed that in response to Staff-4 the Applicants agreed that the ESM should start on October 1, 2024. The Applicants voluntarily proposed this approach to ESM to ensure that ratepayers could not, in any way, be harmed simply because the acquisition of ERHDC was completed as phase 1 prior to the phase 2 amalgamation with NBHDL.

38. OEB Staff also point out an error that was made in the draft accounting order filed in Appendix "F" to the interrogatory responses.[21] A corrected draft accounting order is included as Appendix "A" to these submissions.

39. The Applicants proposal is that the ESM would be disposed of in the first rebasing application following the deferred rebasing period, which is consistent with the response to Staff-5(a)).

40. In addition, the Applicants would be willing to file the results of the ESM annually as part of each IRM application on the understanding that a detailed review and disposition of the ESM would not be considered until the first rebasing application following the deferred rebasing period.

[21] OEB Staff Submissions at pg. 10.

41. For the reasons set forth in the Application and the IRRs and as further discussed above, the Applicants submit that the OEB should grant the relief requested in Section 2 of the Application.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 4TH DAY OF MARCH, 2022

BORDEN LADNER GERVAIS LLP

Per: J Vellone

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John Vellone
Counsel to NBHDL & ERHDC

Appendix "A"

Draft Accounting Order

2435 - Accrued Rate-Payer Benefit (Earnings Sharing Mechanism "ESM")

In its Decision and Order in EB-2021-0312 (the "Decision"), the Ontario Energy Board ("OEB") approved the Applicants proposed Earnings Sharing Mechanism ("ESM") along with the establishment of a new deferral account ("ESM Deferral Account"). The ESM Deferral Account will record 50% of earnings above the 300-basis point deadband that will be shared with ratepayers of "New NBHDL", the company that will be formed upon completion of the approved amalgamation of North Bay Hydro Distribution Ltd. ("NBHDL") and Espanola Regional Hydro Distribution Corporation ("ERHDC").

The account will be established as Account 2435, Accrued Rate-Payer Benefit, and will record the ESM benefits New NBHDL customers will be entitled to beginning October 1, 2024, until April 30, 2027, the year the Applicants have proposed coming forward for rate harmonization in a Cost of Service Application. New NBHDL will record interest on the balance recorded in this deferral account using OEB-prescribed interest rates.

Disposition of balances in this account are subject to review through the first rebasing application of New NBHDL and are expected to be achieved through a rate rider.

Accounting Entries:

New NBHDL will share overearnings 300 basis points above the OEB-approved ROE on a 50:50 basis with ratepayers effective October 1, 2024.

The sample journal entries are provided below:

Dr. 4395 Rate-Payer Benefit Including Interest

Cr. 2435 - Accrued Rate-Payer Benefit

To record 50% of the amounts over the return on equity ceiling that will be returned to ratepayers as part of the Phase 2 MAADs application ESM agreement.

Dr. 4395 Rate-Payer Benefit Including Interest

Cr. 2435 - Accrued Rate-Payer Benefit

To record the carrying charges, at the OEB approved amount, on the opening balance of the monthly principal amount in 2435 - Accrued Rate-Payer Benefit.