Ontario Energy Board | Commission de l'énergie de l'Ontario

Ontario

DECISION AND ORDER

EB-2021-0312

NORTH BAY HYDRO DISTRIBUTION LIMITED AND ESPANOLA REGIONAL HYDRO DISTRIBUTION CORPORATION

Application for approval to amalgamate and continue operations as a single electricity distribution company

BEFORE: Robert Dodds
Presiding Commissioner

Michael Janigan
Commissioner

March 17, 2022

Ontario Energy Board | Commission de l'énergie de l'Ontario

TABLE OF CONTENTS

1 OVERVIEW

This is the Decision and Order of the Ontario Energy Board (OEB) regarding an application (the Application) filed by Espanola Regional Hydro Distribution Corporation (Espanola Hydro) and North Bay Hydro Distribution Ltd. (North Bay Hydro) (collectively, the Applicants) on November 24, 2021. The Applicants requested, pursuant to section 86 of the *Ontario Energy Board Act, 1998* (OEB Act)[1], that the OEB approve a transaction that would allow Espanola Hydro and North Bay Hydro to amalgamate and continue as one corporation operating under the name of North Bay Hydro Distribution Ltd. (referred to herein as New NBH).

As a result of an earlier application in 2019 (the Phase 1 Transaction), both North Bay Hydro and Espanola Hydro became wholly-owned subsidiary corporations of North Bay Hydro Holdings Limited (NBHHL).[2]

The currently proposed transaction for the amalgamation of Espanola Hydro and North Bay Hydro is referred to herein as the Phase 2 Transaction.

The OEB has applied the "no harm" test in assessing this application and finds that the proposed Phase 2 Transaction meets that test. The OEB, therefore, approves the amalgamation of Espanola Hydro and North Bay Hydro into a single electricity distribution company, subject to certain conditions. The OEB also approves the additional requests made by the Applicants as further described in this Decision.

[1] S.O. 1998, c. 15, Schedule B
[2] EB-2019-0015

2 CONTEXT AND PROCESS

2.1 The Applicants

Espanola Hydro is a wholly-owned subsidiary of NBHHL and has a distribution system that serves approximately 3,328 distribution customers in the Town of Espanola and the Township of Sables-Spanish Rivers (specifically the Towns of Espanola, Webbwood and Massey).

North Bay Hydro is also a wholly-owned subsidiary of NBHHL that owns and operates the electricity distribution system that provides service to approximately 24,290 mostly residential and commercial electricity customers in the City of North Bay.

The parent holding corporation, NBHHL, is headquartered in the City of North Bay and is the sole owner of North Bay Hydro Services Inc., North Bay Hydro, Espanola Hydro, and North Bay Hydro Generations Ltd. NBHHL is, in turn, solely owned by the City of North Bay. If approved, the amalgamated entity will serve over 27,000 customers.

2.2 The Application

The Applicants seek OEB approval of the following aspects of the Phase 2 Transaction:

a) Leave for North Bay Hydro and Espanola Hydro to amalgamate and continue as a corporation referred to as New NBH, pursuant to Section 86(1)(c) of the OEB Act

b) Leave to transfer the current and any future rate orders and rate riders of Espanola to New NBH pursuant to Section 18 of the OEB Act

c) Approval for New NBH to continue to track costs to existing deferral and variance accounts

d) An order to amend North Bay Hydro's distribution licence, pursuant to Section 74 of the OEB Act, to include Espanola Hydro's service territory, to be effective on the completion of the amalgamation and to be followed immediately by the cancellation of the distribution licence of Espanola Hydro pursuant to Section 77(5) of the OEB Act.

2.3 The Process

The OEB issued a Notice of Application on December 16, 2021, inviting interested parties to register as intervenors or file a letter of comment with the OEB. On January

28, 2022, the OEB issued Procedural Order No. 1 (PO 1), in which it approved Mr. Donald D. Rennick and School Energy Coalition (SEC) as intervenors. In PO 1 the OEB also established an Issues List and set out the schedule for filing interrogatories, responses to interrogatories and submissions.

On January 31, 2022, Mr. Rennick filed a Notice of Motion (Motion) requesting that the OEB require North Bay Hydro to provide certain information to its board of directors and obtain an updated approval for the amalgamation. The Motion also requested a later date for the filing of interrogatories to allow for the information requested in the Motion to be obtained, examined and for OEB staff and intervenors to request any relevant information and documentation.

The OEB issued a Decision dismissing the Motion without a hearing and found that the Motion was filed at a premature stage in the proceeding and did not demonstrate that the information sought by Mr. Rennick was relevant or would assist the panel in determining the issues in this proceeding.

In accordance with the schedule established in PO 1, interrogatories were posed by intervenors and OEB staff on February 7, 2022, and the Applicants filed their responses to interrogatories on February 15, 2022. Submissions were filed by OEB staff and SEC on February 25, 2022, and by Mr. Rennick on February 27, 2022. The Applicants filed a reply submission on March 4, 2022.

2.3.1 Admissibility of Mr. Rennick's Sur-Reply Submission

On March 7, 2022, Mr. Rennick filed a further submission in response to the Applicants' reply submission, (i.e., a sur-reply submission). On the same date, the Applicants filed a letter requesting that the sur-reply submission be struck from the record, on the basis that there was no provision for such a submission in the schedule approved by the OEB in PO 1. The Applicants stated that Mr. Rennick failed to demonstrate how the Applicants' reply submission raises any new evidence or argument that requires a further reply. In the alternative, the Applicants requested permission to file a further reply submission.

Findings

The OEB finds the sur-reply submission of Mr. Rennick neither meets the procedure for submissions set out in PO 1 nor does it advance any compelling reason for its acceptance. The sur-reply will accordingly not be considered or addressed in this finding.

The OEB notes that there was no procedural order for filing sur-reply by any party nor was it requested by any party. In the ordinary course, where there is no procedural order for sur-reply, a party that seeks to file a sur-reply must bring a motion for leave to do so. Mr. Rennick did not seek leave to file a sur-reply. However, even if leave had been requested, it would not be granted unless the proposed sur-reply is necessary to respond to the Applicants' reply submission.

While the OEB is not bound by previous decisions of the OEB or other tribunals, it agrees with the conditions of acceptance of sur-reply as expressed by another tribunal decision which stated:

> [S]ur-reply submissions should only be provided in limited or exceptional circumstances and are not intended to be an additional opportunity for parties to supplement previous submissions.
>
> Sur-reply submissions may only be necessary when a party has made additional legal arguments or introduced additional issues in reply, provided an inaccurate statement of the law, or an inaccurate statement of facts critical to the determination of the issues in dispute.
>
> Minimal corrections to secondary or tertiary issues that do not otherwise impact the ultimate determination of the issues in dispute, is not a valid reason to file a sur-reply.[3]

[3] *Godber v. Aviva Insurance Company*, Ontario Licence Appeals Tribunal, July 27, 2021, at paragraphs 19-21 CanLII 69333 (ON LAT). See also *E.L. v. Wawnesa Mutual Insurance Company*, Ontario Licence Appeals Tribunal, June 15, 2020, at paragraphs 6-18 CanLII 42668 (ON LAT)

3 REGULATORY PRINCIPLES

3.1 The "No Harm" Test

The OEB applies the "no harm" test in its assessment of merger, acquisition, amalgamation and divestiture (MAAD) applications.[4] The OEB considers whether the "no harm" test is satisfied based on an assessment of the cumulative effect of the transaction on the attainment of its statutory objectives. If the proposed transaction has a positive or neutral effect on the attainment of these objectives, the OEB will approve the application.

The statutory objectives to be considered are those set out in section 1 of the OEB Act.

1. To inform consumers and protect their interests with respect to prices and the adequacy, reliability and quality of electricity service.
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.
3. To promote electricity conservation and demand management in a manner consistent with the policies of the Government of Ontario, including having regard to the consumer's economic circumstances.
4. To facilitate innovation in the electricity sector.

While the OEB has broad statutory objectives, in applying the "no harm" test the OEB's focus is on the objectives that are most directly relevant to the impact of the proposed transaction, namely, price, reliability and quality of electricity service to customers, as well as the cost-effectiveness, economic efficiency and financial viability of the consolidating utilities. The OEB considers this an appropriate approach, given the performance-based regulatory framework under which regulated entities are required to operate and the OEB's existing performance monitoring framework.

[4] The OEB adopted the "no harm" test in a combined proceeding (RP-2005-0018/EB-2005-0234/EB2005-0254/EB-2005-0257) as the relevant test for determining applications for leave to acquire shares or amalgamate under Section 86 of the Act and it has been subsequently applied in applications for consolidation. As prescribed by the OEB's Handbook to Electricity Distributor and Transmitter Consolidations, the OEB has, and will continue to apply its "no harm" test in reviewing consolidation transactions.

3.2 OEB Policy on Rate Making Associated with Consolidations

The OEB has put in place policies on rate-making that provide consolidating distributors with an opportunity to offset transaction costs with savings achieved as a result of the consolidation. The OEB's *Report of the Board on Rate-Making Associated with Distributor Consolidation*, issued on March 26, 2015, (2015 Report) permits consolidating distributors to defer rebasing for up to ten years from the closing of the transaction.[5]

The OEB's *Handbook to Electricity Distributor and Transmitter Consolidations* (MAADs Handbook) provides that the extent of the deferred rebasing period is at the option of the distributor and no supporting evidence is required to justify the selection of the deferred rebasing period. Consolidating entities must, however, select a definitive timeframe for the deferred rebasing period. This is to allow the OEB to assess any proposed departure from this stated plan. When a consolidated entity has opted for a deferred rebasing period, it has committed to a plan based on the circumstances of the consolidation and, if it seeks to amend the deferred rebasing period, the OEB will need to understand whether any change to the proposed rebasing timeframe is in the best interest of customers.[6]

The 2015 Report sets out the rate-setting mechanisms available during the deferred rebasing period and requires consolidating entities that propose to defer rebasing beyond five years to implement an Earnings Sharing Mechanism (ESM) for the period beyond five years to protect customers and ensure that they share in increased benefits from consolidation.

The MAADs Handbook clarifies that rate-setting following a consolidation will not be addressed in an application for approval of a consolidation transaction unless there is a rate proposal that is an integral aspect of the consolidation, such as a temporary rate reduction. Rate-setting for a consolidated entity will be addressed in a separate rate application, in accordance with the rate-setting policies established by the OEB.

The Applicants elected to defer rate rebasing for five years following the completion of the Phase 2 Transaction.

[5] EB-2014-0138
[6] MAADs Handbook, January 19, 2016, pp. 12-13

4 DECISION ON THE ISSUES

The OEB has applied the “no harm” test in assessing the Application and finds that the Phase 2 Transaction meets this test. Therefore, the OEB approves the amalgamation of Espanola Hydro and North Bay Hydro into a single electricity distribution company, New NBH, subject to certain conditions discussed in the sections that follow.

The OEB also approves the additional requests made by the Applicants as further described in this Decision. The sections correspond with the issues per the approved Issues List.[7]

4.1 Application of the “No Harm” Test

In the subsections that follow the OEB sets out its findings with respect to the “no-harm” test and assessment of the effect of the Phase 2 Transaction relative to the following OEB objectives:

- Price, Economic Efficiency and Cost Effectiveness
- Reliability and Quality of Electricity Service
- Financial Viability

4.1.1 Price, Economic Efficiency and Cost Effectiveness

To demonstrate “no harm,” applicants are required to show that there is a reasonable expectation based on underlying cost structures that the costs to serve customers following a consolidation will be no higher than they would otherwise have been.[8] In its review of consolidation proposals, the OEB reviews the underlying cost structures of the consolidating utilities. As distribution rates are based on a distributor’s current and projected costs, the OEB has stated that it is important for the OEB to consider the impact of a transaction on the cost structures of consolidating entities both now and in the future, particularly if there appear to be significant differences in the size or demographics of consolidating distributors.[9]

[7] Schedule “B” of PO 1
[8] MAADs Handbook, p. 7
[9] *Ibid*., p. 6

As stated earlier, both Espanola Hydro and North Bay Hydro are wholly owned by NBHHL. There is no purchase price involved in the Phase 2 Transaction and no associated purchase price premium and these matters were previously addressed in the proceeding for the Phase 1 Transaction.

The Applicants stated that the incremental costs associated with the Phase 2 Transaction are estimated at $300K, with $215K being for transition costs and $85K for transaction costs. The Applicants also stated that these incremental costs will not be recovered from ratepayers.

The Applicants stated that, as a result of the amalgamation, there will be synergies obtained by eliminating duplicate functions currently needed to be done for each of Espanola Hydro and North Bay Hydro. The Applicants stated:

> Over the long-term horizon, this acquisition is anticipated to generate sustainable administrative cost savings as a result of centralizing back-office functions including management, billing, customer service, finance and regulatory functions.[10]

Further elaboration was provided in response to interrogatories 1-Staff-2, SEC-4, SEC-11.

The Applicants stated that ratepayers in Espanola Hydro's rate zone will receive more of the operational benefits initially resulting from the Phase 2 Transaction. These benefits are in the form of improved service performance, such as an extension of North Bay Hydro's SCADA system, and the elimination of back-office costs on a stand-alone basis.

Forecasted synergies and savings are expected to amount to $657K in 2023 and increase to $686K by 2026. The Applicants state that 30% of these synergies would be a direct result of the proposed amalgamation. These are primarily in terms of operating, maintenance and administration (OM&A) costs, although the Applicants note that savings in capital costs are expected in the longer term. Cost savings initially accrue to New NBH and its shareholders and recover the $300K transaction costs discussed earlier.

[10] Application, November 24, 2021, p. 36

OEB staff noted that ratepayers in both rate zones will benefit from the OM&A savings at the time of the first rebasing application for New NBH, forecasted to be for rates effective May 1, 2027.

SEC submitted that it initially had concerns about increased staffing, and associated cost pressures, related to North Bay Hydro assuming the services currently provided by the service agreement between PUC Distribution Inc. (PUC Distribution) and Espanola Hydro (PUC Service Agreement). However, in response to an interrogatory, North Bay Hydro stated that there were no increased staffing pressures. SEC noted that the elimination of the costs for the PUC Service Agreement is a major source of synergies and cost savings resulting from the Phase 2 Transaction. SEC also noted that, while Espanola Hydro ratepayers will see more of the savings, the savings and benefits will accrue to customers in both rate zones by the time of rebasing.

Mr. Rennick submitted that the Applicants had overestimated the forecasted savings, not taking the costs of financing the debt for the purchase of Espanola Hydro into account. Mr. Rennick also submitted that the forecasted OM&A savings are reduced materially by additional staffing that North Bay Hydro forecasted in its last cost of service application to rebase rates. He submitted that the increased staffing forecasted in that rate application is within the scope of the issues. In Mr. Rennick's submission, the OM&A savings should be forecasted to decrease from $686K per year to $207K per year, and the cost per customer for North Bay Hydro would increase from $357.73 (with no amalgamation) to $370.95. Mr. Rennick submitted that the Application be denied.

In reply, the Applicants agreed with the submissions of OEB staff and SEC.

The Applicants disagreed with Mr. Rennick's submissions. With respect to the argument regarding the funding of the debt incurred with the acquisition of Espanola Hydro in the Phase 1 Transaction, the Applicants argued that Mr. Rennick made an incorrect assumption that the debt will be paid off without replacement; they note that it is common business operations to replace retired debt so as to maintain the debt-to-equity (D/E) ratio. They also submitted that the argument about the debt incurred as a result of the Phase 1 Transaction is irrelevant to the current Application, and also note that no new debt is being incurred as a result of the Phase 2 Transaction that is the subject of this Application.

The Applicants also submitted that the increased staffing at North Bay Hydro and associated costs, which were considered and approved by the OEB in North Bay Hydro's last cost of service application, are unrelated to the Phase 2 Transaction. The

Applicants submitted that the increased staffing at North Bay Hydro was needed for operational purposes, regardless of whether or not the amalgamation occurs.

Findings

The OEB finds the costs to the customers of North Bay Hydro or Espanola Hydro will be no higher as a result of the amalgamation than they would have been had it not occurred. The OEB accepts the evidence that the amalgamation is likely to result efficiency gains by the amalgamated utility that should produce lower rates than would have been charged without the merger.

The OEB does not accept the financial analyses of Mr. Rennick, advancing his conclusion that the merger will create increased costs for North Bay Hydro customers. This includes his prediction that there will be increased OM&A costs to North Bay Hydro customers for additional staffing. The relevant staffing costs were addressed and approved in North Bay Hydro’s last cost of service application and are not an issue for this Phase 2 application. Mr. Rennick’s calculation of the adverse effects of the debt financing for the purchase of Espanola is dealt with later in this Decision.

4.1.2 Reliability and Quality of Electricity Service

The MAADs Handbook requires consolidating utilities to indicate the impact that the proposed transaction will have on customers with respect to the quality and reliability of electricity service. In considering the impact of a proposed transaction on the quality and reliability of electricity service, and whether the “no harm” test has been met, the OEB is informed by, among other things, the metrics provided by the distributor in its annual reporting to the OEB and published in its annual scorecard.[11] In the application, the Applicants provided System Average Interruption Duration Index (SAIDI) and System Average Interruption Frequency Index (SAIFI) statistics for Espanola Hydro and North Bay Hydro from 2016 to 2020. This was updated with 2021 SAIDI and SAIFI statistics in response to an interrogatory.

The Applicants stated that a key objective of the proposed amalgamation will be to ensure levels of customer service, safety and reliability that either meet or exceed existing levels in each of the North Bay Hydro and Espanola Hydro service areas.

[11] MAADs Handbook, p. 4

The Applicants noted similarities in the nature of the service territories in terms of weather and terrain, and similar mixes of the customers in the two areas, and stated that these similarities should ease the task of operating as one merged utility.

The Applicants noted that, due to the distance between the North Bay Hydro and Espanola Hydro service territories (about 175 km), they propose that the operations centre in Espanola will remain functional, and with at least one manager, to provide service locally to customers in Espanola, Webbwood and Massey (Espanola Hydro's licensed service territory).

North Bay Hydro plans to extend its SCADA system to the Espanola Hydro service territory. OEB staff submitted that this should result in improved reliability to the customers there, as monitoring of the system will allow for faster detection of and response to system problems when they occur.

Understanding the differences in reliability measurement between Espanola Hydro and North Bay Hydro, SEC nonetheless submitted that:

> [T]he Proposed Transaction presents the Applicants with an opportunity to further improve service reliability in both territories … [and] encourages the Applicants to allocate some of the savings from synergies to invest in areas that improve service reliability.[12]

In reply, the Applicants agreed with the points noted by OEB staff and SEC in their submissions.

Findings

The OEB is satisfied that the amalgamated company, New NBH, will maintain the service quality and reliability standards currently provided by each of the amalgamating utilities. The OEB also expects that New NBH will be able to improve service quality and reliability for both service territories through the planned continuance of operations centre for Espanola Hydro and extension of North Bay Hydro's SCADA system to the Espanola Hydro service territory.

4.1.3 Financial Viability

The MAADs Handbook indicates that the impact of a proposed transaction on the acquiring utility's financial viability for an acquisition, or on the financial viability of the

[12] SEC Submission, p. 3

consolidated entity in the case of a merger or amalgamation, will be assessed. The OEB's primary considerations in this regard are:

- The effect of the purchase price, including any premium paid above the historic (book) value of the assets involved.
- The financing of incremental costs (transaction and integration costs) to implement the consolidation transaction.

The Applicants stated that, since North Bay Hydro and Espanola Hydro are both subsidiary corporations of the same holding company (NBH Holding), the amalgamation is simpler under the Ontario *Business Corporations Act* (OBCA). Further, as a result of the existing common ownership by NBHHL, there is no change in control that would result from the proposed amalgamation. As a result of the common ownership of the merging utilities, there is no purchase price, or associated premium, involved in the Phase 2 Transaction.

OEB staff took no issue with the impact of the Phase 2 Transaction on the financial viability of New NBH, noting the existing common ownership of Espanola Hydro and North Bay Hydro simplifies the amalgamation requirements under the OBCA, results in no change in control, and incurs no purchase price or associated premium.

Mr. Rennick submitted that the D/E ratio for the merged entity, based on the filed pro forma financial statements in the application, would be close to 1.46. Mr. Rennick submitted that this was close to the ratio where lenders would raise concerns regarding further lending, and at what rates and terms. Mr. Rennick noted that the increase in the D/E ratio was due to additional debt incurred for the acquisition of Espanola Hydro as a result of the Phase 1 Transaction.

In reply, the Applicants argued that Mr. Rennick's analysis was untested and flawed, and was based on an assumption that the additional debt taken on with the purchase of Espanola Hydro in the Phase 1 Transaction would be retired without being refinanced "from time-to-time, as would normally be the case (thus maintaining the prescribed debt-to-equity ratio over time)."[13] The Applicants argued that Mr. Rennick's analysis is unrealistic for a capital-intensive firm such as an electricity utility. They further argued that:

---

[13] Reply Submission, p. 3

> 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. [Emphasis in original][14]

The Applicants submitted that Mr. Rennick's analysis is irrelevant as it pertains to the Phase 1 Transaction decided on in the earlier proceeding in 2019, and not to the Phase 2 Transaction that is the subject of the current Application.

The Applicants also submitted that Mr. Rennick's argument that New NBH's forecasted D/E ratio is increasing to 1.46 is flawed. They noted that the response to an interrogatory showed that the D/E ratio based on the 2023 pro forma statements would be 1.26. They further argued that the deduction of goodwill is counter to accepted practice and that Mr. Rennick's analysis should be dismissed.

Findings

The OEB finds that there will be no adverse effects on the financial viability of either the Applicants or the amalgamated company, New NBH, upon completion of the Phase 2 Transaction to amalgamate North Bay Hydro and Espanola Hydro.

The OEB notes that the existing common ownership of Espanola Hydro and North Bay Hydro simplifies the amalgamation requirements under the OBCA, results in no change in control, and incurs no purchase price or associated premium.

The OEB does not accept Mr. Rennick's conclusion that the financing of the debt for the purchase of Espanola will produce additional costs for North Bay Hydro customers that will be greater than any efficiency gains from the merger. This conclusion is primarily based on Mr. Rennick's assumptions derived from the filed pro forma financial statements for 2023 of New NBH. The OEB accepts North Bay's Hydro's reply submission that, in addition to miscalculating the resulting debt to equity ratio, Mr. Rennick's assumptions collide with accepted regulatory practice concerning the utility management of debt and the accounting for the time value of money for cash flows.In any event, the assumptions are also not in scope as they pertain to the transaction approved in Phase 1.

[14] *Ibid*., p. 4

4.2 Directions and Orders from Previous OEB Decisions

In section 1.2 of the Application, the Applicants addressed those items from the 2019 Phase 1 MAADs decision and the 2021 rebasing applications of each of Espanola Hydro and North Bay Hydro,[15] that are pertinent to the current Application. These items are summarized as follows:

1. As a condition of the Settlement Agreement in Espanola Hydro's rebasing application for 2021 rates Espanola Hydro must, within two years of the final rate order in that rate application, either file an application for a merger with North Bay Hydro or file a new cost of service application to rebase Espanola Hydro's rates. In the event that neither condition was met, Espanola Hydro would forego a formulaic Price Cap IR rate adjustment for 2022.
2. The Phase 1 MAADs decision ordered Espanola Hydro and North Bay Hydro to conduct an analysis of accounting policy differences between the two utilities and bring forward a proposal in the next cost of service application.
3. In the Phase 1 MAADs proceeding and in the North Bay Hydro rate application to rebase rates for 2021, the OEB deferred consideration of the Earnings Sharing Mechanism (ESM) set to commence at the beginning of the sixth year after completion of the Phase 1 MAADs transaction.

This Application satisfies the first outstanding item. The second item (accounting policy) was addressed in Espanola Hydro's 2021 cost of service application.[16]

The only outstanding issue is the third item (ESM) which had been deferred from previous applications. As noted above, in its decision on the Phase 1 Transaction, the OEB deferred consideration of the ESM to a subsequent rate application.[17] The matter of the ESM was again considered in North Bay Hydro's rate application to rebase its 2021 electricity distribution rates. However, the OEB's decision in the 2021 cost of service rate application further deferred consideration of the ESM to this application.[18]

The Applicants have made a proposal for the ESM in this Application.

[15] EB-2020-0020 and EB-2020-0043
[16] EB-2020-0020
[17] EB-2019-0015, Decision and Order
[18] EB-2020-0043, Decision and Order, September 9, 2021, p. 34

OEB staff submitted that first two outstanding items had been dealt with and made submissions on the ESM proposal under Issue 4.4, which is discussed further in this Decision.

Findings

The OEB accepts that two of the three directions and orders from the 2019 Phase 1 MAADs decision and the 2021 rebasing applications for Espanola Hydro and North Bay Hydro have been previously addressed. The third item that is still outstanding, the Earnings Sharing Mechanism (ESM), is addressed under Issue 4.4 in this Decision.

4.3 Service Agreement Between Espanola Hydro and North Bay Hydro

Prior to the application regarding the Phase 1 Transaction, Espanola Hydro had entered into the PUC Service Agreement, which was effective until February 28, 2022, and would not be extended or renewed.

Between March 1, 2022 and the date when the Phase 2 Transaction is executed (and assuming OEB approval of this Application), North Bay Hydro proposes to execute a service agreement with Espanola Hydro that is:

- equivalent to the PUC Service Agreement; and
- Affiliate Relationships Code for Distributors and Transmitters (ARC) compliant.

In response to an interrogatory, the Applicants provided additional detail on the proposed service agreement, the differences from the PUC Service Agreement and the changes necessary for compliance with the ARC. A copy of the current PUC Service Agreement was filed as an appendix to the interrogatory responses, as is the proposed service agreement between Espanola Hydro and North Bay Hydro, effective January 1, 2022.[19]

OEB staff submitted that the proposed service agreement between Espanola Hydro and North Bay Hydro, for the period until the entities amalgamate (assuming approval of the Application), is appropriate and compliant with OEB policies.

[19] Appendix “A” for the PUC Distribution Inc. Service Agreement, and Appendix “B” for the 2022 Service Agreement between Espanola Hydro and North Bay Hydro.

In its submission, SEC noted its initial concern about North Bay Hydro having to increase its staffing in taking over the services currently being provided by PUC Distribution to Espanola Hydro. However, SEC submitted that its concerns were addressed by responses to interrogatories and that retirement of the PUC Service Agreement would be the main source of synergies and OM&A savings up until rebasing.

Findings

The OEB finds that the proposed service agreement between Espanola Hydro and North Bay Hydro, for the period until the entities amalgamate, is appropriate and compliant with OEB policies.

4.4 Earnings Sharing Mechanism

The MAADs Handbook requires that consolidating utilities that propose to defer rebasing beyond a five-year period implement an ESM for the period beyond five years, where excess earning above 300 basis points of the consolidated entity's annual return on equity (ROE) is shared 50:50 with customers.

While the Applicants are electing a five-year deferred rebasing period as part of this Application, the start of the ESM is determined from when the Phase 1 Transaction was completed on October 1, 2019.

4.4.1 Earnings Sharing Mechanism Proposal

The Applicants proposed the following for the ESM:

- The ESM would commence on October 1, 2025, and continue until the effective date of rebased distribution rates for New NBH as a result of a cost of service application proposed for 2027.
- The ESM would be asymmetric, with over earnings 300 basis points above the allowed ROE to be shared 50:50 between New NBH's ratepayers and shareholders.

In response to an interrogatory, the Applicants revised the start date for the ESM to October 1, 2024, corresponding with the start of the sixth year following the completion of the Phase 1 Transaction.

OEB staff submitted that, with the revised start date for the ESM, the revised proposal was compliant with OEB policy. OEB staff also noted that the ESM proposal creates two stub periods at the beginning and the end of the deferred rebasing period from October

1, 2024 to April 30, 2027, based on the Applicants' proposal that New NBH would rebase distribution rates to be effective May 1, 2027. OEB staff supported the Applicants' proposal for proportional calculation of any overearnings during the stub periods based on the calendar year earnings in which the stub period occurred.

In reply, the Applicants filed a revised draft Accounting Order for the ESM that aligned with the response to interrogatory 5-Staff-5 a). The Applicants proposed to report the ESM account balance annually in subsequent Price Cap IR applicants, with a detailed review and disposition of the ESM account balance at the time of the next cost of service application to rebase rates.

Findings

The OEB concludes that the Applicants' proposal is consistent with the MAADs Handbook and approves the Applicants' proposal for an ESM to be implemented starting year six of the deferred rebasing following the amalgamation. Year 6 of the ESM commences October 1, 2024, corresponding with the start of the sixth year following the completion of the Phase 1 Transaction in 2019. The Applicants are required to:

a) Report the ESM account balance annually in in subsequent Price Cap IR applications, with a detailed review and disposition of the ESM account balance at the time of the next cost of service application to rebase rates

b) Share excess earnings with customers annually. Adjustments to revenue and expenses will be reviewed at the time of disposition of shared savings.

c) Implement proportional calculation of any overearnings during the stub periods based on the calendar year earnings in which the stub period occurs.

4.4.2 Draft Accounting Order

The Applicants filed a draft accounting order for the ESM entries in response to interrogatories. In the draft accounting order, the Applicants state that the disposition of material balances in this account is subject to review through the annual IRM process.

The Applicants proposed two sample accounting entries, with one sample entry to record any realized over-earning in the proposed ESM account in any given year, and with the other sample entry to record the carrying charges on the principal balance of the ESM account, using the OEB's prescribed interest rates.

OEB staff submitted that the reference to materiality is not necessary or appropriate, noting that the MAADs Handbook states that "the ESM is designed to protect customers and ensure that they share in any increased benefits from consolidation during the deferred rebasing period".[20] OEB staff submitted that any balance in the proposed ESM account should be subject to review through the annual rate-setting process.

Otherwise, OEB staff stated that it had no concerns with the proposed sample journal entries in the draft accounting order and the proposed disposition method (i.e., on an annual basis through the rate applications process). OEB staff submitted that the proposed Uniform System of Accounts (4395 Rate-Payer Benefit Including Interest and 2435 Accrued Rate-Payer Benefit) are appropriate accounts to record any earnings sharing amounts.

As noted above, the Applicants filed a revised draft accounting order that has removed the reference to the materiality for the ESM and provides for a detailed review and disposition of the account balance at New NBH's next rebasing application, scheduled for rates effective May 1, 2027.[21]

Findings

The OEB accepts the proposed sample journal entries in the draft accounting order and the proposed disposition method. Any balance in the proposed ESM account should be subject to review through the annual rate-setting process.

4.5 Next Rebasing Period

In response to an interrogatory from OEB staff, the Applicants proposed that the next rebasing for New NBH, following deferred rebasing, would be for rates effective May 1, 2027.

No parties opposed the proposal for rebased rates to be effective for May 1, 2027. OEB staff submitted that an application for rates rebased through a cost of service application for that effective date should be filed in the summer of 2026.

Findings

The OEB approves the deferred rebasing period requested by the Applicants.

[20] *Handbook to Electricity Distributor and Transmitter Consolidations*, January 19, 2016, page 16
[21] EB-2020-0020, Settlement Proposal, page 42

The OEB's MAADs Handbook specifies that the term of the deferred rebasing is at the option of the distributor up to ten years, and an applicant does not need to file evidence in support of the deferral period it chooses. The OEB concludes that the Applicants' proposal is consistent with the OEB's policy, and no party has established a compelling reason to depart from that policy.

4.6 Rate-setting and Accounting Matters

The following sections of the Decision address the Applicants' proposals with respect to rate-setting and accounting matters, including the treatment of deferral and variance accounts.

4.6.1 Rates

The Applicants proposed that the current approved Tariff of Rates and Charges of both North Bay Hydro and Espanola Hydro be transferred to New NBH upon completion of the Phase 2 Transaction. The service areas of the legacy North Bay Hydro and Espanola Hydro will be treated as separate rate zones until rebasing, at which time the Applicants also propose that rate harmonization over the rate zones will be considered.

OEB staff submitted that the Applicants' proposals are consistent with OEB policy regarding rate-making considerations resulting from MAADs applications.

OEB staff also noted that Espanola Hydro has not completed the transition of moving customers in the Residential Customer Class to a fully fixed Monthly Service Charge, but that this should be completed (i.e., for 2026 distribution rates) as part of a 5-year plan agreed to as part of the Settlement Proposal accepted by the OEB in Espanola Hydro's 2021 cost of service application.[22]

Findings

The OEB finds that the Applicants' proposals are consistent with OEB policy regarding rate-making considerations resulting from MAADs applications, and approves the Applicants' proposals that:

a) the current approved Tariff of Rates and Charges of both North Bay Hydro and Espanola Hydro be transferred to New NBH upon completion of the Phase 2 transaction.

[22] EB-2020-0020, Decision and Rate Order, June 10, 2021, Schedule B: Settlement Proposal, pp. 28-29 of 65

b) The service areas of the legacy North Bay Hydro and Espanola Hydro be treated as separate rate zones until rebasing, at which time rate harmonization over the rate zones will be considered

c) New NBH complete the transition of moving customers in the Residential Customer Class of the Espanola Hydro rate zone to a fully fixed Monthly Service Charge by the next rebasing.

4.6.2 Accounting Policies

In the decision on the Phase 1 Transaction, the OEB stated that:

> The Applicant's preliminary review has not identified material differences in the underlying accounting policies between North Bay Hydro and Espanola Hydro. The Applicant is ordered to complete its analysis of accounting policies and bring forward a detailed proposal as part of its cost of service rate application.[23]

The settlement proposal filed in Espanola Hydro's 2021 cost of service application and approved by the OEB stated that:

> The Parties agree that ERHDC has responded appropriately to the OEB's order in EB-2019-0015 that ERHDC complete an analysis on the differences in accounting policies between ERHDC and NBHDL. The Parties agree that nothing further is required as a result of this analysis on accounting policies.[24]

OEB staff submitted that any accounting policy differences have been addressed in Espanola Hydro's last rebasing application.

Findings

The OEB notes that analyses to identify material differences in the underlying accounting policies between North Bay Hydro and Espanola Hydro have been conducted as part of the Phase 1 Transaction and Espanola Hydro's last rebasing application and is satisfied that any accounting policy differences have been adequately addressed.

[23] EB-2019-0015, Decision and Order, August 22, 2019, page 27
[24] EB-2020-0020, Settlement Proposal, page 42

4.6.3 Deferral and Variance Accounts

The Applicants requested OEB approval for New NBH to continue to track costs and revenues in existing deferral and variance accounts (DVAs). This would also be separated by rate zones for the legacy Espanola Hydro and North Bay Hydro service areas.

In responding to an OEB staff interrogatory on the notion of combining the Group 1 DVAs for New NBH, the Applicants stated that New NBH will have separate revenue and expense accounts for settlement purposes for the North Bay and Espanola service areas as commodity cost variances for each service area are settled with different suppliers. Currently Espanola Hydro settles with Hydro One while North Bay Hydro settles with the IESO and, even after merging, the separate settlement processes will continue, at least until rebasing.

As a result, OEB staff supported the separation of Group 1 accounts as proposed by the Applicants because the proposal is more practical and suitable for the two service areas within the New NBH, although the situation may need re-examination at rebasing, particularly if rate harmonization is being proposed.

The Applicants stated that they intend to continue to track Group 2 accounts separately, except for Account 1592 – sub account CCA (capital cost allowance) Changes. In that change, the Applicants noted that, with amalgamation, taxes would be paid by New NBH as a single entity. As such, it would be very difficult to track Account 1592 – sub account CCA Changes.

The proposed combined Account 1592 for tracking purposes for New NBH would be for the purpose of determining the tax implications of the tax expense of New NBH versus the combined tax expense allowance approved in the decisions for North Bay Hydro’s and Espanola Hydro’s 2021 cost of service applications. The 2022 stub periods for Espanola Hydro and North Bay Hydro would also be taken into consideration. The intent would then be to file a harmonized rate rider, if applicable.

In its submission, OEB staff noted that, in their respective 2021 rate applications, North Bay Hydro and Espanola Hydro rebased under the Accelerated Incentive Investment Program (AIIP) rules and disposed the Account 1592 sub-account balances up to the year ended December 31, 2019. The AIIP program is scheduled to start phasing out in 2024, which OEB staff submitted may result in under-recovery of Payment in Lieu of Taxes (PILs) by the time the merged utility is scheduled to rebase in 2027.

OEB staff stated that it was not clear how the proposed methodology for tracking the variances for the new amalgamated company in a single Account 1592 sub-account would work, or whether the proposal is appropriate. OEB staff noted that, to date, distributors have had Account 1592 balances approved for disposition by the OEB calculated as follows:

1) the difference between the CCA deductions that would have been claimed had the tax rules in place at the time of rebasing been applied, and the actual CCA claimed using revised tax rules, based on actual capital expenditures made in the year, or

2) the difference between the CCA deductions that were approved using tax rules in place at the time of rebasing and the CCA deductions that would have been approved had the revised tax rules been applied in the last cost of service application, based on the OEB-approved capital expenditures.

OEB staff submitted that neither scenario above is consistent with the Applicants' proposal (actual CCA claimed using revised tax rules vs. approved CCA deductions using the prior tax rules – in essence, a true-up of CCA). OEB staff further submitted that there was not sufficient opportunity to test the reasonableness of the proposed methodology in this proceeding, and that these details should be deferred to the proceeding in which disposition of Account 1592 – sub account CCA Changes is being sought.

OEB staff submitted that the 2020 and 2021 CCA differences that have been tracked and recorded in North Bay Hydro's and Espanola Hydro's separate accounts to date, can be disposed of in New NBH's 2027 rebasing application. OEB staff stated that it took no issue with the proposal to track and record CCA differences in a combined account for New NBH following amalgamation. However, OEB staff submitted that the OEB would be assisted in making its decision on a rate application in which the disposition of DVA balances are being sought if, as part of that application, New NBH would provide the appropriate 1592 sub-account calculations and balances separately for North Bay Hydro and Espanola Hydro for the pre-amalgamation period and for New NBH for the post-amalgamation period.

The Applicants did not address the rates and accounting policy matters in their reply submission.

Findings

The OEB grants leave for New NBH to continue to track costs and revenues to the existing Group 1 and Group 2 deferral and variance accounts (DVAs) with conditions as described herein.

Group 1 deferral and variance accounts will have separate revenue and expense accounts for settlement purposes for the North Bay Hydro and Espanola Hydro service areas since commodity cost variances for each service area are settled with different suppliers. The OEB notes the situation may need re-examination at rebasing, particularly if rate harmonization is being proposed

Group 2 accounts will continue to be tracked separately, except for Account 1592 – sub account CCA (capital cost allowance) Changes which will be combined since taxes will be paid by New NBH as a single entity. The OEB requires that the 2020 and 2021 CCA differences that have been tracked and recorded in North Bay Hydro's and Espanola Hydro's separate accounts to date, be disposed of in New NBH's 2027 rebasing application. The OEB notes it would be assisted in that application if New NBH provides the appropriate 1592 sub-account calculations and balances separately for North Bay Hydro and Espanola Hydro for the pre-amalgamation period and for New NBH for the post-amalgamation period.

5 LICENCE

As noted earlier in the Overview, the Applicants requested an order to amend North Bay Hydro's distribution licence to include Espanola Hydro's service territory, to be effective on the completion of the amalgamation and to be followed immediately by the cancellation of the distribution licence of Espanola Hydro.

OEB staff and the intervenors did not make submissions on the requested approval to amend North Bay Hydro's distribution licence, which would continue for New NBH.

Findings

The OEB approves the Applicants' request to amend North Bay Hydro's distribution licence to include Espanola Hydro's service territory, to be effective on the completion of the amalgamation and to be followed immediately by the cancellation of the distribution licence of Espanola Hydro.

6 ORDER

THE ONTARIO ENERGY BOARD ORDERS THAT:

1. North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation are granted leave to amalgamate and continue as North Bay Hydro Distribution Limited

2. The leave granted in paragraph 1 shall expire 18 months from the date of this Decision and Order. If the transaction has not been completed by that date, a new application will be required in order for the transaction to proceed

3. North Bay Hydro Distribution Limited shall notify the OEB of the completion of the transaction referred to in paragraph 1 above

4. Once the notice referred to in paragraph 3 has been provided to the OEB, the OEB will transfer the rate order of Espanola Regional Hydro Distribution Corporation to North Bay Hydro Distribution Limited

5. Once the notice referred to in paragraph 3 has been provided to the OEB, the OEB will issue the amended Electricity Distribution Licence (ED-2003-0024) to North Bay Hydro Distribution Limited to include the service areas formerly served by Espanola Regional Hydro Distribution Corporation

6. When the OEB issues the amended Electricity Distribution Licence to North Bay Hydro Distribution Limited, it will cancel the Electricity Distribution Licence of Espanola Regional Hydro Distribution Corporation (ED-2002-0502)

7. North Bay Hydro Distribution Limited is approved to continue, after the amalgamation, to track costs to the deferral and variance accounts currently approved by the OEB for each of North Bay Hydro Distribution Corporation and Espanola Regional Hydro Distribution Corporation

8. The accounting order filed in Appendix A for Account 2435 - Accrued Rate-Payer Benefit relating to the ESM is approved.

Cost Claims

9. The School Energy Coalition and Mr. Donald D. Rennick shall file with the OEB and forward to North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation their respective cost claim no later than **April 7, 2022**.

10. North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation with the OEB and forward to the School Energy Coalition and Mr. Donald D. Rennick any objections to the claimed costs of the School Energy Coalition and Mr. Rennick by **April 14, 2022**.

11. The School Energy Coalition and Mr. Donald D. Rennick shall file with the OEB and forward to North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation any responses to any objections for its cost claim by **April 21, 2022**.

12. North Bay Hydro Distribution Limited and Espanola Regional Hydro Distribution Corporation shall pay the OEB's costs of and incidental to, this proceeding immediately upon receipt of the OEB's invoice.

Parties are responsible for ensuring that any documents they file with the OEB, such as applicant and intervenor evidence, interrogatories and responses to interrogatories or any other type of document, **do not include personal information** (as that phrase is defined in the *Freedom of Information and Protection of Privacy Act*), unless filed in accordance with rule 9A of the OEB's Rules of Practice and Procedure.

Please quote file number, **EB-2021-0312,** for all materials filed and submit them in searchable/unrestricted PDF format with a digital signature through the OEB's online filing portal.

- Filings should clearly state the sender's name, postal address, telephone number and e-mail address.
- Please use the document naming conventions and document submission standards outlined in the Regulatory Electronic Submission System (RESS) Document Guidelines found at the File documents online page on the OEB's website.
- Parties are encouraged to use RESS. Those who have not yet set up an account, or require assistance using the online filing portal can contact registrar@oeb.ca for assistance.

- Cost claims are filed through the OEB's online filing portal. Please visit the File documents online page of the OEB's website for more information. All participants shall download a copy of their submitted cost claim and serve it on all required parties as per the Practice Direction on Cost Awards.

All communications should be directed to the attention of the Registrar and be received by end of business, 4:45 p.m., on the required date.

With respect to distribution lists for all electronic correspondence and materials related to this proceeding, parties must include the Case Manager, Keith Ritchie at Keith.Ritchie@oeb.ca and OEB Counsel, Ljuba Djurdjevic at Ljuba.Djurdjevic@oeb.ca.

Email: registrar@oeb.ca
Tel: 1-877-632-2727 (Toll free)

DATED at Toronto March 17, 2022

ONTARIO ENERGY BOARD

Nancy Marconi

Digitally signed by Nancy Marconi
Date: 2022.03.17 13:50:12 -04'00'

Nancy Marconi
Registrar

SCHEDULE A

DECISION AND ORDER

NORTH BAY HYDRO DISTRIBUTION LIMITED AND ESPANOLA REGIONAL HYDRO DISTRIBUTION CORPORATION

EB-2021-0312

MARCH 17, 2022

Accounting Order

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

In its Decision and Order in EB-2021-0312 (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. (North Bay Hydro) and Espanola Regional Hydro Distribution Corporation (Espanola Hydro).

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.