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

BY EMAIL

November 4, 2022

Nancy Marconi
Registrar
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4
Registrar@oeb.ca

Dear Ms. Marconi:

Re: Ontario Energy Board (OEB) Staff Submission
Kingston Hydro Corporation
Cost of Service
OEB File Number: EB-2022-0044

Please find attached OEB staff's submission in the above referenced proceeding, pursuant to the OEB's October 24, 2022 letter.

Yours truly,

Vince Mazzone
Digitally signed by Vince Mazzone
Date: 2022.11.04 11:40:24 -04'00'

Vince Mazzone
Advisor – Application Policy & Conservation

Encl.

cc: All parties in EB-2022-0044

ONTARIO ENERGY BOARD

OEB Staff Submission

Kingston Hydro Corporation

Cost of Service Application

EB-2022-0044

November 4, 2022

Introduction

Kingston Hydro Corporation (Kingston Hydro) filed a Cost of Service application with the Ontario Energy Board (OEB) on June 17, 2022, under section 78 of the *Ontario Energy Board Act, 1998* seeking approval for the rates that Kingston Hydro charges for electricity distribution, effective January 1, 2023.

The OEB issued an approved issues list for this proceeding on August 16, 2022. A settlement conference took place from September 28, 2022 to September 30, 2022. Kingston Hydro filed a settlement proposal representing a complete settlement of all issues on October 28, 2022 (the Settlement Proposal). The parties to the Settlement Proposal are Kingston Hydro and the approved intervenors in the proceeding: Consumers Council of Canada, School Energy Coalition, and Vulnerable Energy Consumers Coalition (the Parties). OEB staff participated in the settlement conference but is not a party to the Settlement Proposal

If the Settlement Proposal is approved, a typical residential customer with a monthly consumption of 750 kWh would see a distribution charge increase of $1.47, or 5.4%.

This submission is based on the status of the record at the time of the filing of the Settlement Proposal and reflects observations that arise from OEB staff's review of the evidence and the Settlement Proposal. It is intended to assist the OEB in deciding on whether to approve the Settlement Proposal.

Settlement Proposal

OEB staff has reviewed the Settlement Proposal in the context of the objectives of the *Renewed Regulatory Framework*[1] (RRF), the *Handbook for Utility Rate Applications*[2], applicable OEB policies, relevant OEB decisions, and the OEB's statutory obligations. OEB staff submits that the Settlement Proposal reflects a reasonable evaluation of Kingston Hydro's planned outcomes in this proceeding and appropriate consideration of the relevant issues and ensures that there are sufficient resources (financing, labour, investment and materials) to allow Kingston Hydro to achieve its identified outcomes in the five years of the plan from 2023 to 2027.

OEB staff further submits that the Settlement Proposal and that the outcomes arising from the OEB's approval of the Settlement Proposal would reflect the public interest and would result in just and reasonable rates for customers.

Below, OEB staff provides specific submissions on certain issues established by the OEB:

- Issue 1.1 – Capital
- Issue 1.2 – Operating, Maintenance and Administration
- Issue 2.0 – Revenue Requirement
- Issue 3.0 – Load Forecast, Cost Allocation and Rate Design
- Issue 4.0 – Accounting
- Issue 5.1 – Effective Date
- Issue 5.2 – OEB Directives from Previous Custom IR Application

Issue 1.1 – Capital

In its application, Kingston Hydro proposed a total net capital expenditure of $3.23M for the 2023 test year. As part of the Settlement Proposal, the Parties agreed to an envelope reduction of $140k to the proposed net capital expenditure. In addition, Kingston Hydro committed to the following measures:

- Establish targets for certain metrics of the Distribution System Plan (DSP) in its next IRM application for the 2024-2027 period.
- Revise the targets for SAIDI and SAIFI excluding loss of supply and major events

[1] Report of the Board – Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach, October 18, 2012.
[2] Handbook for Utility Rate Applications, October 13, 2016.

to 1.19 and 1.005, respectively.
- Provide additional details in its next DSP filing on the assets identified as "flagged for action" and, in particular, information and details (i.e., type of assets, quantity of assets) on actual assets replaced over the historical period and assets planned to be replaced over the five-year forecast period in the next DSP.

OEB staff supports the agreement reached by the Parties on capital items.

Issue 1.2 – Operation, Maintenance and Administration (OM&A)

The Parties agreed to total OM&A spending of $8.0M, a reduction of $165k for the 2023 test year from the proposed OM&A in the application. This represents an increase of $13.8% from the 2016 OEB-approved OM&A actual spending, or an annual growth rate of approximately 2% per year. It is expected that Kingston Hydro will move to a Group 2 productivity rating during all years of its IRM term. OEB staff submits that the proposed OM&A expenses, as agreed to in the Settlement Proposal, are reasonable.

Issue 2.0 – Revenue Requirement

The Parties agreed to a service revenue requirement of $15.2M and a base revenue requirement of $14.4M. These values reflect a reduction of $140k in 2023 capital expenditures and a reduction of $165k from OM&A compared to Kingston Hydro's application proposal. The values also reflects changes to depreciation, cost of capital, working capital allowance and payments in lieu of taxes. Table 2.2A – 2023 Revenue Deficiency of the Settlement Proposal shows the change in revenue requirement between Kingston Hydro's original application and the Settlement Proposal.

Cost of Capital

The Parties accept that the cost of capital calculations have been appropriately determined in accordance with OEB policies and practices, subject to one debt instrument[3] being adjusted to the lower of the 2023 deemed debt rate and the actual rate of 5.87%, and another debt instrument[4] being adjusted to the lower of the 2023 deemed debt rate and 5.05%.

Payment in Lieu of Corporate Taxes (PILs) – Accelerated Capital Cost Allowance

Bill C-97 introduced the Accelerated Investment Incentive program (AIIP), which

[3] Number 1 in Table 2.1A of the Settlement Proposal
[4] Number 15 in Table 2.1A of the Settlement proposal

provides for a first-year increase in capital cost allowance (CCA) deductions on eligible capital assets acquired after November 20, 2018. The AIIP is expected to be phased out starting in 2024, and fully phased out in 2028.

In its July 25, 2019, letter titled *Accounting Direction Regarding Bill C-97 and Other Changes in Regulatory or Legislated Tax Rules for Capital Cost Allowance* (CCA Letter), the OEB provided accounting direction on the treatment of the impacts from accelerated CCA resulting from the AIIP. The OEB established a separate sub-account, Account 1592 - PILs and Tax Variances, Sub-account CCA Changes to track the impact of any differences that result from the CCA change to the tax rate or rules that were used to determine the tax amount that underpins rates.

Account 1592

The Parties agreed to Kingston Hydro's calculation of the CCA differences that are accumulated in Account 1592, Sub-account CCA Changes, from January 1, 2019 to December 31, 2022. Kingston Hydro confirmed that no amounts for the stub period November 21, 2018 to December 31, 2018 were included in this sub-account and in the Deferral and Variance Account (DVA) Continuity Schedule, as the impact of the accelerated CCA amounts was not claimed on Kingston Hydro's 2018 tax return.[5]

Kingston Hydro compared the CCA on the actual (or forecast, as applicable) capital additions in the respective period under the legacy rule to the accelerated CCA on the same capital additions in the respective period under the AIIP. The calculated sub-account credit balance of $532,437 represents the full revenue requirement impact of the application of accelerated CCA as of December 31, 2022.

The Parties agreed that 100% of the revenue requirement impact is to be returned to Kingston Hydro's ratepayers. OEB staff does not object to this approach, given the CCA Letter states that "determinations as to the appropriate disposition methodology will be made at the time of each Utility's cost-based application". In addition, OEB staff notes that a refund of 100% of the sub-account to ratepayers has previously been approved by the OEB in a prior proceeding[6] and accepted by the OEB in settlement proposals of various proceedings.[7]

[5] 6-Staff-67
[6] Enbridge Gas Inc. Deferral and Variance Account Disposition and Earnings Sharing Mechanism Decision and Order, May 6, 2021, EB-2020-0134.
[7] Hydro Ottawa 2021 Custom IR Decision and Order, EB-2019-0261, November 19, 2020, Waterloo North Hydro Inc. 2021 Cost of Service Decision and Rate Order, EB-2020-0059, December 10, 2020, Brantford Power 2022 Cost of Service Decision and Rate Order EB-2021-0009, October 28, 2021, Canadian Niagara Power Inc. 2022 Cost of Service Decision and Rate Order, December 16, 2021, Corrected February 3, 2022, EB-2021-0011.

Smoothing Mechanism

The CCA Letter also indicated that utilities were to reflect any impacts arising from CCA rule changes in their cost-based applications for 2020 rates and beyond. The CCA Letter also indicated that the OEB may consider a smoothing mechanism to address any timing differences that could lead to volatility in tax deductions over the rate-setting term. The *Chapter 2 Filing Requirements for Electricity Distributors* further state that the OEB will assess smoothing proposals on a case-by-case basis. If the OEB approves the smoothing proposal, the distributor's use of (or access to) Account 1592, to record the impacts of the specific CCA changes contemplated in the smoothing proposal, will no longer be applicable.[8]

In the current application, Kingston Hydro proposed a five-year smoothing adjustment to CCA that is reflected in the 2023 test year PILs provision to address the phasing out of AIIP. Kingston Hydro has incorporated a five-year smoothing method of CCA to reflect the fact that the CCA is gradually declining from the high point in 2023, through to the phase-out period by 2027. The Parties agreed that a smoothing adjustment of a debit amount of $182,540 is to be added to the 2023 test year taxable income.

The Parties noted that while they do not necessarily agree on the methodology used by Kingston Hydro to determine the PILs smoothing adjustment, the Parties agreed that the resulting $182,540 addition to the 2023 test year taxable income is appropriate. OEB staff notes that the smoothing methodology used by Kingston Hydro is different than those accepted by the OEB in settlement proposals of other proceedings. In its pre-filed evidence, Kingston Hydro outlined the steps it used for its PILs smoothing adjustment.[9]

OEB staff does not take issue with Kingston Hydro's smoothing proposal. In OEB staff's view, the agreed-upon smoothing adjustment calculation is one of the appropriate methods to calculate a smoothing adjustment to address the phase-out of AIIP.

The Parties also agreed that no new entries will be recorded in Account 1592, PILs and Tax Variances, Sub-account CCA Changes, subsequent to December 31, 2022, unless there are further changes to the current tax laws and rules governing CCA that are not contemplated in the current proceeding, or if the OEB orders otherwise.

[8] Filing Requirements for Electricity Distribution Rate Applications - 2022 Edition for 2023 Rate Applications, Chapter 2 Cost of Service, April 18, 2022, p. 39 & 40
[9] Exhibit 6, Tab 2, Schedule 1, Page 5

OEB staff agrees with this approach. In OEB staff's view, the intent of a smoothing adjustment is to address the change in CCA rules resulting from Bill C-97 upfront in the current application, instead of capturing the impact of those changes in rules as they occur during the IRM period. Therefore, OEB staff agrees that the 1592 sub-account would no longer be needed for the 2023 to 2027 period, unless there are further changes to CCA rules that were not contemplated in the calculation of the smoothing adjustment.

Tax Appeal

The Ministry of Finance has reassessed Kingston Hydro's 2014 CCA claim for smart meters, removing the classification of smart meters from Class 8 and reclassifying them into Class 47. Kingston Hydro has appealed the reassessment by the Ministry of Finance. If Kingston Hydro is not successful in its appeal, it proposed to recalculate the 2023 CCA claim and include the impacts of the difference between the original claim and the confirmed Ministry reassessment in a sub-account of Account 1592 for future disposition.

However, the Parties agreed that no DVA will be established to capture any PILs-related impacts related to the tax appeal, in the event that Kingston Hydro is unsuccessful in its appeal. Kingston Hydro will bear this risk.

The Parties acknowledged and agreed that Kingston Hydro intends to update the CCA class treatment as part of its next cost of service application and the approach could materially change based on the outcome of the appeal.

OEB staff submits that no DVA should be established to capture any PILs-related impacts related to the appeal if Kingston Hydro is unsuccessful in its appeal. OEB staff notes that establishing a DVA in the current proceeding would trigger rate retroactivity concerns because the reassessment relates to a past period (i.e., 2014).

Issue 3.0 Load Forecast, Cost Allocation and Rate Design

<u>Load Forecast</u>

The Parties agreed to the proposed load forecast subject to the following changes:

1. The COVID Adjustment variable in the test year be reduced. The initial application applied a 50% adjustment to the COVID variables in 2023 to reflect the declining impacts of COVID. The Parties agreed to a 35% adjustment to the

Residential class and a 17.5% adjustment for the General Service < 50 kW, General Service 50 to 4,999 kW, and Large Use rate classes.
2. For the General Service < 50 kW and General Service 50 to 4,999 kW rate classes, August 2022 actuals will be used for the 2023 customer forecast.

OEB staff does not have any concerns with the proposed load forecast of 693,867 MWh, 934,199 kW, and 34,104 customers and connections as shown in Table 3.1A of the Settlement Proposal. Relative to the initial application amounts, this reflects an increase of 7,799 MWh and 21,277 kW. OEB staff submits that the agreed-upon load and customer connection forecasts are appropriate.

Cost Allocation

The Parties agreed to increase the revenue-to-cost ratio for Street Lighting to 80% and Large Use to 85%, the minimum target for these rate classes, as well as an offsetting decrease for GS<50 kW rate class. With these changes, the Parties accepted that Kingston Hydro's proposals on cost allocation and revenue-to-cost ratios are appropriate.

OEB staff has no concern with the cost allocation as agreed to by the Parties.

Rate Design

The current fixed charge for the Large Use rate class is above the ceiling.[10,11] Kingston Hydro proposed, and Parties agreed that the fixed charges for this rate class would remain at their current levels. In all other rate classes, it is proposed that the fixed-variable split be maintained at its current level.

OEB staff has no concern with the proposed rate design.

Retail Transmission Service Rates (RTSRs) and Low Voltage Rates

Kingston Hydro initially proposed to recover a forecasted total LV expense of $1,496,622. This was based on the average low voltage cost for the most recent five-year historical period.

Parties agreed that 2022 Hydro One rates should be applied to 2021 actual volume

[10] The minimum system with peak load carrying capability from the cost allocation model, which is commonly referred to as the ceiling for fixed charges.
[11] Ontario Energy Board Filing Requirements for Electricity Distribution Rate Applications – 2022 Edition for 2023 Rate Applications- Chapter 2, section 2.8.1.

revising the low voltage cost to $1,367,944.

OEB staff has no concern with the proposed RTSRs and Low Voltage rates as shown in Table 3.4A and 3.4B of the Settlement Proposal.

Issue 4.0 Accounting

For the purposes of settlement, the Parties accepted that all impacts of any changes in accounting standards, policies, estimates and adjustments have been properly identified and recorded, and the rate-making treatment of each of these impacts is appropriate. OEB staff does not take issue with this element of the Settlement Proposal.

DVAs

Kingston Hydro proposed to dispose of the following DVA balances as of December 31, 2021 and forecasted interest through to December 31, 2022:

- Group 1 DVAs of a total debit balance of $688,961
- Group 2 DVAs of a total credit balance of $325,505

Some of the Group 2 DVA balances also include forecasted principal amounts for the period of January 1, 2022 to December 31, 2022.[12]

Kingston Hydro proposed to dispose of these balances over a one-year period.

In the Settlement Proposal, the Parties agreed to dispose of the Group 1 and Group 2 balances, as proposed by Kingston Hydro. The Parties also agreed that any amounts previously disposed of on an interim basis in prior proceedings shall be considered as disposed on a final basis.

The Parties agreed to the continuance and discontinuance of certain Group 1 and Group 2 DVAs, as set out in the Settlement Proposal.[13]

OEB staff supports the disposition of Group 1 and Group 2 balances, as proposed by Kingston Hydro and agreed to the Parties. Disposition of these balances over a one-year period is consistent with OEB policy.[14] OEB staff also submits that it is appropriate that any amounts previously disposed of on an interim basis, be considered as disposed

[12] Settlement Proposal, October 28, 2022, p. 39
[13] Settlement Proposal, October 28, 2022, p. 43
[14] EB-2008-0046, Report of the Board on Electricity Distributors' Deferral and Variance Account Review Initiative (EDDVAR), July 31, 2009, p. 24

on a final basis, given the supporting evidence substantiating these balances.[15]

OEB staff submits that the continuance and discontinuance of certain Group 1 and Group 2 DVAs, as set out in the Settlement Proposal, is appropriate.

OEB staff's submission on the above-noted forecasted 2022 Group 2 principal amounts is described below.

Group 2 DVAs

The Parties agreed that Kingston Hydro will not be seeking recovery of the balances in Account 1509, Impacts Arising from the COVID-19 Emergency, and Account 1508, OEB Cost Assessment Account. These accounts will be zeroed out and closed. OEB staff supports this approach.

OEB staff notes that, typically, audited balances are disposed, but there are exceptions to this requirement. For example, in the disposition of retail service charge related variance accounts and the Account 1508 sub-account for pole attachment charges, the OEB may consider disposing forecasted amounts up to the effective date of rebased rates.[16]

OEB staff's view is that there are regulatory efficiencies to be gained and less intergenerational inequity by disposing the forecasted 2022 principal balances in certain accounts in the current application.[17] OEB staff submits that this approach is preferable to disposing the 2022 audited balances of these accounts in Kingston Hydro's next cost of service proceeding (which is expected for 2028 rates).

[15] For example, to address issues raised in prior proceedings regarding Accounts 1588 and 1589 balances, an OEB Inspection was recently completed. At Exhibit 9, Tab 3, Schedule 1, Page 2, Kingston Hydro stated that "there were no required changes to any of Kingston Hydro's balances for any years that were approved on an interim basis" as a result of the OEB Inspection of Accounts 1588 and 1589. The OEB Inspection Report was filed at Exhibit 9, Tab 3, Schedule 1, Attachment 1.
[16] Filing Requirements For Electricity Distribution Rate Applications - 2022 Edition for 2023 Rate Applications, Chapter 2 Cost of Service, April 18, 2022, p. 51 & 63
[17] Settlement Proposal, October 28, 2022, p. 39

- Account 1508, Other Regulatory Assets, Specific Service Charge Variance
- Account 1508, Other Regulatory Assets, Revenue Requirement Differential Variance Account related to Capital Additions
- Account 1508, Other Regulatory Assets, OPEB Forecast Cash vs. Forecast Accrual Differential Deferral Account
- Account 1518, Retail Cost Variance Account – Retail
- Account 1548, Retail Cost Variance Account – STR
- Account 1568, LRAM Variance Account
- Account 1592, PILs and Tax Variance, Sub-account CCA Changes

Pension, OPEB Policy and DVAs

The Parties agreed with Kingston Hydro establishing the change to the accrual basis from the cash basis for Other Post-employment Benefits (OPEBs), and establishing the following Group 2 account as of the proposed effective date of new rates of January 1, 2023.

Account 1522:
- Pension & OPEB Forecast Accrual versus Actual Cash Payment Differential
- Pension & OPEB Forecast Accrual versus Actual Cash Payment Differential Contra Account
- Pension & OPEB Forecast Accrual versus Actual Cash Payment Differential Carrying Charges

The Parties also agreed that Kingston Hydro will follow the guidance contained in the *Report of The Ontario Energy Board: Regulatory Treatment of Pension and Other Post-employment Benefits (OPEBs) Costs* (OEB Report) issued September 14, 2017 for distributors following the accrual accounting method for OPEBs.[18]

OEB staff does not take issue with this element of the Settlement Proposal, given that the OEB Report established the use of the accrual accounting method as the default method for pension and OPEB amounts in cost-based applications.[19] OEB staff also submits that the establishment of Account 1522 sub-accounts effective January 1, 2023 is appropriate, given that the OEB Report states that this account will be effective upon a transition to the accrual method (if approved) as of the date of a utility's next cost-based rate order.[20]

Lost Revenue Adjustment Mechanism Variance Account

Kingston Hydro is proposing to dispose of its updated Lost Revenue Adjustment Mechanism Variance Account (LRAMVA) balance of $278k, including carrying charges. The balance is comprised of savings and persistence of 2015-2020 Conservation & Demand Management (CDM) program activity. In the Settlement Proposal, the Parties agreed to dispose of the updated LRAMVA balance proposed by Kingston Hydro. The Parties also agreed to a disposition period of one-year. If disposition is approved, Kingston Hydro would have a zero balance in the LRAMVA.

[18] EB-2015-0040
[19] EB-2015-0040, *Report of The Ontario Energy Board: Regulatory Treatment of Pension and Other Post-employment Benefits (OPEBs) Costs*, September 14, 2017, p. 2
[20] Ibid, p. 2, 11, 12

OEB staff has no concerns with the updated LRAMVA balance proposed for disposition. The LRAMVA will not be discontinued, in the event that Kingston Hydro requests the use of the LRAMVA for a CDM activity in a future application, which the OEB will consider on a case-by-case basis.

Issue 5.1 – Effective Date

The Parties agreed that an effective date of January 1, 2023 is appropriate.

OEB staff has no concerns with an effective date of January 1, 2023 for Kingston Hydro's rates for 2023.

Issue 5.2 – OEB Directives from Previous Custom IR Application

In the Settlement Proposal in Kingston Hydro's 2016 Custom IR Application, Kingston Hydro agreed "…to develop meaningful metrics/targets and to define outcome reporting". Kingston Hydro retained a consultant (Metsco) to prepare a report on these metrics, selected some of the metrics and reported the associated outcomes in its DSP. Specifically, the Metsco report identified three categories of measures: Customer-Oriented Performance, Planning and Execution Efficiency and Effectiveness, and Equipment Specific Performance.

As part of the Settlement Proposal, the Parties agreed that Kingston Hydro responded appropriately to all relevant OEB directions from previous rate proceedings. Kingston Hydro agreed to establish targets for the metrics as discussed in Issue 1.1. OEB staff has no concerns with how Kingston Hydro addressed the prior directive.

~ All of which is respectfully submitted ~