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

BY EMAIL

September 1, 2023

Ms. 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
Niagara-on-the-Lake Hydro Inc.
2024 Cost of Service Application
OEB File Number: EB-2023-0041

Please find attached OEB staff's submission in the above referenced proceeding, pursuant to Procedural Order No. 1.

Yours truly,

Narisa Jotiban

Digitally signed by Narisa Jotiban
Date: 2023.09.01 10:06:06 -04'00'

Narisa Jotiban
Advisor – Electricity Distribution: Major Rate Applications & Consolidations

Encl.

cc: All parties in EB-2023-0041

ONTARIO ENERGY BOARD

OEB Staff Submission

Niagara-on-the-Lake Hydro Inc.

Cost of Service Application

EB-2023-0041

September 1, 2023

1. Introduction

This is OEB staff's submission on a settlement proposal filed by Niagara-on-the-Lake Hydro Inc. (Niagara-on-the-Lake Hydro) related to its application for January 1, 2024 electricity distribution rates (Application). The settlement proposal represents a complete settlement on all issues on the OEB approved issues list.

The settlement proposal was arrived at during a settlement conference held from August 2, 2023 to August 3, 2023. The parties to the settlement proposal include Niagara-on-the-Lake Hydro and all approved intervenors, namely: School Energy Coalition (SEC) and Vulnerable Energy Consumers Coalition (VECC) (collectively, the Parties). OEB staff attended the settlement conference; however, it 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 monthly distribution charge increase of $4.69 (3.9%).[1]

[1] Including taxes and the Ontario Electricity Rebate

2. Overview

OEB staff submits that the settlement proposal is in the public interest and the accompanying explanation and rationale is adequate to support the settlement proposal. OEB staff further submits that the settlement proposal would result in just and reasonable rates for the customers of Niagara-on-the-Lake Hydro.

OEB staff's position was developed in consideration of the objectives of the *Renewed Regulatory Framework*[2] (RRF), the *Handbook for Utility Rate Applications*[3], applicable OEB policies, relevant OEB decisions, and the OEB's statutory obligations.

This submission provides reasons for OEB staff's position by commenting on each issue as they appear on the OEB-approved issues list, as shown below.[4]

- Issue 1: Capital Spending and Rate Base
- Issue 2: Operating, Maintenance and Administration (OM&A)
- Issue 3: Cost of Capital, PILs, and Revenue Requirement
- Issue 4: Load Forecast
- Issue 5: Cost Allocation, Rate Design, and Other Charges
- Issue 6: Deferral and Variance Accounts
- Issue 7: Other

[2] Report of the Board – *Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach*, October 18, 2012
[3] *Handbook for Utility Rate Applications*, October 13, 2016
[4] EB-2023-0041: OEB approved Issues List

3. OEB Staff Submissions on the Issues

The OEB-approved issues list included seven issues, each of which contains one or more sub-issues. OEB staff's submission is categorized in accordance with the approved issues list.

Issue 1: Capital Spending and Rate Base

1.1 Are the proposed capital expenditures and in-service additions appropriate?

OEB staff supports the proposed capital expenditures and in-service additions. Niagara-on-the-Lake Hydro's application requested a capital in-service additions budget for the 2024 Test Year of $2.0M. Through settlement, the Parties agreed to a reduction of 2024 opening net fixed assets of $250k in buildings. Parties also agreed to an envelope reduction of $144k (7%) for 2024, resulting in a proposed in-service additions budget for the 2024 Test Year of $1.8M.[5]

As described in the settlement proposal, the reduction to capital in-service additions is intended to reflect the construction schedule of the new building over the 2023 to 2024 period and match the average of Niagara-on-the-Lake Hydro's capital expenditures over the five-year forecast period.[6]

OEB staff agrees with the pacing strategy proposed by the Parties and further submits the proposed in-service additions budget is sufficient for Niagara-on-the-Lake Hydro to continue to operate its system reliably.

1.2 Are the proposed rate base and depreciation amounts appropriate?

OEB staff supports the proposed rate base and depreciation amounts which have been calculated in accordance with the agreements reached through the settlement process, as further described below.

The proposed 2024 rate base is $35.2M, a $0.3M (1%) reduction from the amount included in the Application.[7] The following adjustments agreed to by the Parties contribute to the adjusted rate base: capital additions, depreciation, and allowance for working capital.

Issue 2: OM&A

2.1 Are the proposed OM&A expenditures appropriate?

OEB staff considers the agreement reached by the Parties with respect to 2024 OM&A expenses reasonable.

[5] Settlement Proposal, pp. 7-8
[6] Settlement Proposal, p. 8
[7] Settlement Proposal, Table 6, p. 9

Niagara-on-the-Lake Hydro proposed total OM&A expenses of $3.6M for the 2024 Test Year in the Application, an increase of 34% (or 6% compounded annually) compared to the 2019 OEB-approved OM&A spending of $2.7M. Niagara-on-the-Lake Hydro stated that the OM&A cost increases have been driven by inflation, growth, increasing complexity of operations, and escalation of certain costs above inflation.[8]

Through settlement, the Parties have agreed to an envelope reduction of $125k to Niagara-on-the-Lake Hydro's proposed 2024 OM&A expenses, which amounts to $3.4M as seen in Table 8 of the settlement proposal. As stated in the settlement proposal, the reduction takes into consideration that Niagara-on-the-Lake Hydro moved from Cohort 3 (the third most efficiency group) productivity rating to Cohort 2 (the second most efficiency group) in 2021 and remained in Cohort 2 in 2022 and also provides sufficient OM&A spending to maintain a safe and reliable distribution system.[9]

The revised 2024 OM&A spending represents an increase of 29% (or 5% compounded annually) compared to the 2019 OEB-approved OM&A amount. OEB staff notes that although the 5% annual compound increase in the revised OM&A is relatively high, Niagara-on-the-Lake Hydro has made several efforts to mitigate rising costs since the 2019 rebasing application. From a cost efficiency perspective, Niagara-on-the-Lake Hydro moved up to Cohort 2 in 2021 from Cohort 3 as a result of improved cost management.[10] By comparing historical OM&A costs with other utilities in Ontario, Niagara-on-the-Lake Hydro's average OM&A costs (by category) per customer from the 2017 to 2021 were lower than or on-par with the industry average.[11]

In the context of the overall settlement proposal, OEB staff submits that the envelope reduction of $125k in OM&A is reasonable. OEB staff further notes that the settled OM&A envelope should ensure that Niagara-on-the-Lake Hydro has the resources to maintain a safe and reliable distribution system.

2.2 Is the proposed shared services cost allocation methodology and the quantum appropriate?

OEB staff supports the proposed shared services cost allocation methodology and quantum.

Issue 3: Cost of Capital, PILs, and Revenue Requirement

3.1 Is the proposed cost of capital (interest on debt, return on equity) and capital structure appropriate?

OEB staff supports the proposed cost of capital and capital structure as summarized in Tables 9 and 10 of the settlement proposal on the basis that the cost of capital

[8] Exhibit 4, pp. 7-9
[9] Settlement Proposal, p. 10
[10] Empirical Research in Support of Incentive Rate-Setting: 2022 Benchmarking Update, July 2023
[11] APB Unit Cost Calculations: 2021 Results, March 27, 2023

calculation has been appropriately determined in accordance with OEB policies and practices, including being based on the OEB's latest cost of capital parameters for 2023.[12] In addition, OEB staff supports Niagara-on-the-Lake Hydro's approach in using the OEB's deemed long-term debt rate for an original promissory note with the Town of Niagara-on-the-Lake since it is consistent with that approved in the 2019 Cost of Service filing.[13]

As part of the agreements reached through the settlement process, the Parties have agreed on the use of the OEB approved deemed capital structure of 4% short term debt, 56% long term debt and 40% equity. In addition, the Parties have also agreed that the return on equity applicable to Niagara-on-the-Lake Hydro's cost of capital, the rate of interest applicable to the short-term debt and the rate of interest applicable to the balance of the Original Promissory Note will be updated to the OEB's approved rates for 2024.[14]

OEB staff submits that the agreed upon capital structure and updates to the cost of capital are appropriate.

3.2 Is the proposed PILs (or Tax) amount appropriate?

OEB staff does not take issue with the forecast PILs expense of $116,981 as agreed to by the Parties. The PILs expense reflects the application of the small business deduction on a utility stand-alone basis, consistent with the requirements set out in the OEB's PILs Workform. In the settlement proposal, Niagara-on-the-Lake Hydro noted concerns with the application of the small business deduction on a stand-alone basis and stated that it will send a letter to the OEB regarding its concerns. OEB staff is of the view that this submission is not the appropriate forum to discuss the merits of OEB policy.[15]

OEB staff notes that the forecast PILs does not reflect accelerated capital cost allowance (CCA), but reflects CCA using the legacy half year rule.[16] Niagara-on-the-Lake Hydro indicated that it has not opted into the program to accelerate CCA due to fairness to ratepayers. Niagara-on-the-Lake Hydro stated that to the extent that accelerated tax deferrals are achieved today, these taxes will still have to be paid in the future and that obligation will fall on future ratepayers.[17] The OEB generally requires CCA to be maximized.[18] However, OEB staff notes that the total CCA deductions

[12] OEB Letter – Cost of Capital Parameters, October 22, 2022
[13] Exhibit 5, p. 10
[14] Settlement Proposal, p. 11
[15] Settlement Proposal, pp. 13-14
[16] Accelerated CCA was introduced through the Accelerated Investment Incentive program (AIIP), to provide for a first-year increase in CCA deductions on eligible capital assets acquired after November 20, 2018. The AIIP is being phased out starting in 2024, and is expected to be fully phased out by 2028.
[17] Exhibit 6, p.13
[18] 2024 Income Tax/PILs Workform, Integrity Checks tab

available over the life of an asset remains the same regardless of whether accelerated CCA is implemented or not. Therefore, OEB staff agrees with Niagara-on-the-Lake Hydro that any taxes that are deferred today as a result of accelerated CCA, will be incurred by future ratepayers. As a result, in the context of settlement OEB staff does not take issue with Niagara-on-the-Lake Hydro's PILs methodology.

3.3 Is the proposed Other Revenue forecast appropriate?

OEB staff supports the revised 2024 Test Year other revenue of $616k, an increase of $7k compared to $609k included in the Application (Table 12 of the settlement proposal).

Through settlement, the Parties agreed to an adjustment to a pole rental charge which was revised during interrogatories to reflect the OEB inflation factor of 4.8% for 2024 (from 3.7% in the Application). This adjustment increases the pole rental charge to $37.78 from 36.05 in the Application[19], and reflects in the increase of $7k in other operating revenues.[20]

3.4 Have all impacts of any changes in accounting standards, policies, estimates and adjustments been properly identified and recorded, and is the rate-making treatment of each of these impacts appropriate?

OEB staff does not take issue with the settlement proposal agreed to by the Parties for this element of the settlement.

The Parties agree that the impacts of any changes in accounting standards, policies, estimates and adjustments have been properly identified and recorded, and the rate-making treatment of these impacts is appropriate.

3.5 Is the proposed calculation of the Revenue Requirement appropriate?

OEB staff supports the proposed revenue requirement which has been calculated in accordance with the agreements reached through the settlement process.

The Parties agreed to a service revenue requirement of $7.2M and a base revenue requirement of $6.5M.[21] These values reflect a reduction in the 2024 Test Year capital and OM&A expenditures of $144k and $125k, respectively, comparatively to the Application. The values also reflect changes to revenue offsets, depreciation, cost of capital, working capital allowance, and PILs. Table 1 of the settlement proposal shows the change in revenue requirement between the Application, interrogatories, and the settlement proposal.

OEB staff considers the combined resultant bill impacts of the proposed revenue

[19] 8-VECC-50 IRR
[20] Chapter 2 Appendices, Appendix 2-H
[21] Settlement Proposal, Table 13, p.15

requirement and the proposed mitigation to be reasonable. Although no rate mitigation proposals are required under OEB policies, Niagara-on-the-Lake Hydro proposed to recover its distribution rate increases over two years for each of its customer classes (see issue 5.6).

As shown at Table 2 of the settlement proposal, the proposal results in bill impacts with mitigation for all customer classes range between 2.3% and 7.8%. For residential and general service < 50kW rate classes, the monthly bill impacts are 3.9% on a total bill basis.

Issue 4: Load Forecast

4.1 Is the proposed load forecast methodologies and the resulting load forecasts appropriate?

OEB staff submits that the adjustments included in the settlement agreement are reasonable.

The Parties agreed to introduce a COVID variable to the regression equations, and to increase the Street Lighting customer connections by 46. A formula error was also identified and corrected.[22]

OEB staff supports the proposed consumption, demand and customer forecasts of 257 GWh, 285 MW, and 12,457 respectively (Tables 14 and 15 of the settlement proposal). Relative to the Application, this reflects an increase of 5 GWh for consumption and 3 MW for demand. The proposed customer forecast increases by 89 compared to the Application.

Issue 5: Cost Allocation, Rate Design, and Other Charges

5.1 Are the proposed cost allocation methodology, allocations, and revenue-to-cost ratios, appropriate?

The Parties agreed that the cost allocation proposed by Niagara-on-the-Lake Hydro is appropriate. Niagara-on-the-Lake Hydro continued to rely on its previous load profiles, initially produced by Hydro One based on 2004 data in support of its 2006 Cost Allocation Information Filing. The Parties agreed that it would update its load profiles using updated customer data. OEB staff agrees that Niagara-on-the-Lake Hydro should be required to update its load profiles at its next rebasing proceeding and should take any necessary steps now to ensure that it will be able to do so.

The revenue-to-cost ratios for all rate classes except the Street Lighting rate class are within the OEB prescribed ranges. The Street Lighting revenue-to-cost ratio is 1.4036, while the prescribed range is 0.8 to 1.2.[23] The Parties agreed that no revenue-to-cost

[22] Settlement Proposal, p. 16
[23] Settlement Proposal, Table 16, p. 18

ratios would be adjusted. Niagara-on-the-Lake Hydro states that it received approval for the proposed rates and impacts from its Board of Directors, which includes the mayor, a town councilor, and the CAO of the Town of Niagara-on-the-Lake. The town of Niagara-on-the-Lake owns 96.7% of the Street Lighting connections.[24]

OEB staff has no concerns with the cost allocation methodology as agreed to by the Parties, or with the resulting revenue-to-cost ratios.

5.2 Is the proposed rate design, including fixed/variable splits, appropriate?

The Parties agreed that Niagara-on-the-Lake Hydro would maintain the fixed charge for rate classes where the fixed charge is already above the ceiling as calculated by the cost allocation model, and maintain the fixed/variable split where that results in a fixed charge below the ceiling. In the case of Unmetered Scattered Load class, the Parties agreed that the fixed charge would be increased to the ceiling, and that this reflects a smaller percentage increase than the variable charge.[25]

OEB staff supports the proposed rate design, including the fixed/variable splits.

5.3 Are the proposed Retail Transmission Service Rates (RTSR) appropriate?

OEB staff supports the RTSR rates as agreed to by the Parties.

5.4 Are the proposed loss factors appropriate?

OEB staff supports the proposed loss factors as shown in the settlement proposal.

OEB staff notes that the proposed loss factor is essentially unchanged, increasing from 1.0373 to 1.0374.

5.5 Are the Specific Service Charges and Retail Service Charges appropriate?

The Parties agreed that the charges for special meter reads, meter disputes, reconnections following non-payment of account, and service calls for customer owned equipment would be updated. Niagara-on-the-Lake Hydro provided cost information supporting the updated charges.[26]

OEB staff has no concerns with Niagara-on-the-Lake Hydro's proposed Specific Service Charges and Retail Service charges.

5.6 Are rate mitigation proposals required and appropriate?

Although rate mitigation proposals were not required, the Parties agreed that Niagara-on-the-Lake Hydro would implement its distribution rate increases over two years. The

[24] IRR 7-Staff-50
[25] Settlement Proposal, p. 20
[26] IRR 8-Staff-54

Parties agreed that updated rates would be calculated using the OEB models. These rates would be mitigated by only applying 50% of the increase to the distribution rates in 2024. The calculated rates prior to mitigation would then be proposed to be used as the starting point before any incentive rate making adjustment in Niagara-on-the-Lake's next proceeding. Niagara-on-the-Lake Hydro estimated that the proposed mitigation will result in a savings of $228,674 to customers in 2024, which will be borne by Niagara-on-the-Lake Hydro.[27]

OEB staff is not opposed to the agreed upon rate mitigation but notes that the eventual 2025 rate change will be higher than without the proposed mitigation.

Issue 6: Deferral and Variance Accounts

6.1 Are the proposals for deferral and variance accounts, including the balances in the existing accounts and their disposition, requests for new accounts, requests for discontinuation of accounts, and the continuation of existing accounts, appropriate?

OEB staff supports the settlement proposal reached by the Parties relating to deferral and variance accounts (DVAs).

In the settlement proposal, the Parties agreed to the disposition of the following DVA balances as of December 31, 2022 and forecasted interest through to December 31, 2023, over a one-year disposition period.

- Group 1 DVAs of a total debit balance of $823,799
- Group 2 DVAs of a total debit balance of $292,981

OEB staff notes that the Parties have agreed to the disposition of Account 1576 – Accounting Changes for a debit amount of $145,840 on a final basis. The balance represents a residual balance resulting from the difference between the balance previously approved for disposition and the resulting actual rate riders refunded to customers.[28] OEB staff notes that typically, residual balances for Account 1576 have not been disposed. Per the OEB's guidance for this account, upon disposition, the approved balance remains in Account 1576 and is drawn down.[29] It is not transferred to Account 1595 - Disposition and Recovery/Refund of Regulatory Balances where variances between forecasted and actual billing determinants used to calculate rate riders are trued-up upon disposition. However, OEB staff notes that the relevant rate rider was effective from 2014 to 2019,[30] and the lengthy disposition period would have magnified any variances between forecast and actual billing determinants resulting in a larger residual. OEB staff also notes that the balance in the account is material to Niagara-on-the-Lake

[27] Settlement Proposal, pp. 23-24
[28] IRR 9-Staff-60
[29] Accounting Procedures Handbook, March 2015 Guidance #6
[30] IRR 9-Staff-60

Hydro. Therefore, in the context of settlement, OEB staff does not oppose the disposition of Niagara-on-the-Lake Hydro's Account 1576 balance.

Issue 7: Other

7.1 Is the proposed effective date appropriate?

OEB staff supports the settlement proposal with respect to Niagara-on-the-Lake Hydro's requested effective date of January 1, 2024.

7.2 Has the applicant responded appropriately to all relevant OEB directions from previous proceedings?

OEB staff supports the Parties' view that Niagara-on-the-Lake Hydro has responded appropriately to all previous OEB directions.

7.3 Is the applicant's proposal to have the Large Use customer Retail Transmission Service Rates automatically change to match changes in the Uniform Transmission Rates appropriate?

Niagara-on-the-Lake Hydro had its Large Use customer RTSRs adjusted to match the Uniform Transmission Rates (UTRs) in its 2022 Rate Modification Application.[31] In this proceeding, the Parties agreed that Niagara-on-the-Lake Hydro will reset its RTSRs to match the UTRs, and that it will continue to make applications as needed to update the Large Use customer RTSRs.

OEB staff has no concerns with the proposal for updating the Large Use customer RTSRs.[32]

~All of which is respectfully submitted~

[31] EB-2022-0158
[32] Settlement Proposal, p. 27