E.L.K. Energy Inc.

February 08, 2024

Nancy Marconi
Board Secretary
Ontario Energy Board
PO Box 2319
2300 Yonge Street, Suite 2700
Toronto ON M4P 1E4

Dear Ms. Marconi:

Re: E.L.K. Energy Inc. 2024 Incentive Regulation Mechanism ("IRM") Distribution Rate Application EB-2023-0013

In accordance with the instructions released by the Ontario Energy Board ("the Board") in Procedural Order No 1 dated November 24, 2023 E.L.K. Energy Inc. ("E.L.K. Energy") hereby submits its Reply Submission

An electronic copy of this Application has been filed with the Board RESS Filing System. . The filing includes the Reply Argument; and live versions of the following models or files:

1. ELK-2024-IRM-Rate-Generator-Model_20240208_Reply: Updated IRM Rate Generator Model
2. E.L.K_2024_ACM_ICM_Model_ELK 20240208_Reply Sub: E.L.K. Energy's proposed smoothing represented in the OEB's ACM/ICM Model

Regards

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E.L.K. Energy Inc.
EB-2023-0013

Reply Submission

Introduction

E.L.K. Energy Inc. ("E.L.K. Energy") filed an Incentive Rate-setting Mechanism ("IRM") application for 2024 distribution rates on October 11, 2023 with the Ontario Energy Board ("OEB"), inclusive of two Incremental Capital Module ("ICM") funding requests, and two Z Factor claims. The ICM requests relate to two bucket trucks and six Viper reclosing switches which are or will be placed into service in 2024 ("ICM Projects"), while the two Z Factor claims relate to a severe ice storm in February of 2023 ("Ice Storm"), and a severe thunderstorm in July of 2023 ("Thunderstorm") (together, "Z Factor Claims").

On December 7, 2023, OEB Staff and Vulnerable Energy Consumers Coalition ("VECC") submitted interrogatories regarding E.L.K. Energy's evidence, to which E.L.K. Energy provided responses on January 11, 2024.

On January 25 and 26, 2024, OEB Staff and VECC made Submissions regarding E.L.K. Energy's IRM application, ICM requests, and Z Factor Claims. The following are E.L.K. Energy's Reply Submissions responding to the comments of OEB Staff and VECC. E.L.K. Energy's Reply Submission can be summarized as follows:

- OEB Staff accept E.L.K. Energy's request for a 2024 distribution rate increase based on the approved Price Cap methodology and support E.L.K. Energy's proposal to defer disposition of Group 1 Deferral and Variance Accounts ("DVAs"), while VECC does not comment on these issues. E.L.K. Energy submits its 2024 IRM adjustment should be approved as filed;

- OEB Staff and VECC agree that E.L.K. Energy's Z Factor claims both meet the OEB's 3-part test of Causation, Materiality, and Prudence. Both recommend against Z Factor funding for poles replaced during storm restoration efforts which were otherwise planned for replacement as part of E.L.K. Energy's standard pole replacement program. E.L.K. Energy accepts this recommendation and agrees with the specific reductions to Z Factor funding proposed by OEB Staff. OEB Staff also raise the treatment of PILs in the determination of Z Factor capital-related revenue requirement, as further addressed below. Inclusive of the pole replacement adjustment, E.L.K. Energy submits the Z Factor Claims should be approved;

- OEB Staff and VECC agree that E.L.K. Energy's ICM Projects both meet the OEB's 3-part test of Need, Materiality, and Prudence. However, OEB Staff submissions disagree with E.L.K. Energy's proposed treatment of PILs in determining ICM (and Z Factor) funding, while VECC makes no submission on this issue. E.L.K. Energy disagrees with OEB Staff's PILs submissions, which call for unjustly stringent application of ICM policies[1] as written, raise an irrelevant comparison to another distributor and proceeding, propose the OEB engage in retroactive rate-making, and most

[1] EB-2014-0219, Report of the Board - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014

importantly ignore the OEB's statutory objective to facilitate the maintenance of a financially viable electricity industry;

- OEB Staff's submission encouraged E.L.K. Energy to propose a Capital Cost Allowance ("CCA") smoothing mechanism as an alternative means to addressing the impact of PILs in determining ICM funding. E.L.K. Energy has proposed a mechanism which is directly responsive to OEB Staff's recommendation and addresses E.L.K. Energy funding needs, while preserving CCA tax benefits;

- E.L.K. Energy submits the ICM Projects should be approved as meeting the OEB's 3-part test, and ICM rate riders should be approved inclusive of E.L.K. Energy's proposed CCA smoothing mechanism.

E.L.K. Energy's Reply Submission has been organized into the following sections:

- IRM Adjustment;
- Z Factor Claims;
- ICM Requests; and,
- PILs Issue & Capital Cost Allowance ("CCA") Smoothing.

IRM Adjustment

With respect to E.L.K. Energy's applied-for Price Cap IRM adjustment and treatment of Group 1 Deferral and Variance Accounts ("DVAs"), neither OEB Staff nor VECC raised objections to approval of the application as filed. OEB Staff identified no concerns with E.L.K. Energy's applied-for Price Cap adjustment,[2] and further accepted that E.L.K. Energy is not in a position to dispose of Group 1 DVAs at this time.[3] OEB Staff submitted that E.L.K. Energy should take "preemptive measures to ensure that audits are completed in a timely manner, avoiding further delays in the disposition of accounts."[4] E.L.K. Energy takes no issue with this recommendation, and notes OEB Staff's acknowledgement of the steps it has taken to ensure adequate staffing through a Management Services Agreement with Entegrus Inc.

VECC made no submissions regarding the IRM components of E.L.K. Energy's application, limiting its comments to E.L.K. Energy's ICM requests and Z Factor claims.

Given neither OEB Staff nor VECC expressed concerns with these elements of E.L.K. Energy's application, E.L.K. Energy submits the OEB should approve its IRM Price Cap escalation and proposal to defer Group 1 DVA disposition as filed. As requested by OEB Staff,[5] E.L.K. Energy has updated its 2024 IRM Model to incorporate final Retail Transmission Service Rates ("RTSRs"), and an updated Rural and Remote Rate

[2] OEB Staff Submission, p.1
[3] Ibid., p.2
[4] Ibid., p.3
[5] Ibid., p.1

Protection ("RRRP") rate. The updated model also incorporates revised Z Factor rate riders, consistent with E.L.K. Energy's submissions on this matter below.

Z Factor Claims

Both OEB Staff and VECC submitted that the Ice Storm and Thunderstorm events met the OEB's 3-part Z Factor test of Causation, Materiality, and Prudence. However, both OEB Staff[6] and VECC[7] noted that 3 of the 10 poles replaced as a result of the Ice Storm, and 1 of the 6 poles replaced as a result of the Thunderstorm, were scheduled for replacement as part of E.L.K. Energy's regular pole replacement program. Both parties recommended the capital costs relied upon to calculate capital-related revenue requirement and resulting Z Factor rate riders should be reduced to remove the costs of these poles.

E.L.K. Energy accepts the Submissions of OEB Staff and VECC that 3 of the 10 poles affected by the Ice Storm and 1 of the 6 poles affected by the Thunderstorm were scheduled for replacement as part of the pole inspection capital plan. E.L.K. Energy accepts OEB Staff's proposed reductions, which are: (i) a 30% reduction in the costs associated with the 10 poles replaced as part of the Ice Storm; and (ii) a 16.7% reduction in the cost associated with the 6 poles replaced as part of the Thunderstorm. E.L.K. Energy has implemented reductions to the capital costs associated with the Ice Storm and Thunderstorm totalling $4,720 per OEB Staff's submission, with subsequent capital-related revenue requirement reductions incorporated into the Z Factor rate riders.[8]

OEB Staff also raised issues with respect to E.L.K. Energy's treatment of PILs in the calculation of capital-related revenue requirement resulting from the Ice Storm and Thunderstorm, though OEB Staff note "the amounts of the negative PILs adjustments are not material, and the impacts on the ratepayers are minimal compared to the overall Z factor request."[9] E.L.K. Energy addresses this matter later in this Reply Submission, concurrent with the same issue as it pertains to the ICM Projects.

Given that OEB Staff and VECC are generally supportive of the Z Factor claims, E.L.K. Energy submits the OEB should approve its Ice Storm and Thunderstorm Z Factor claims and associated rate riders, as revised in the attached IRM Model.

[6] Ibid., p.7
[7] VECC Submission, p.3,4
[8] OEB Staff, p.7
[9] Ibid., p.10

ICM Requests

OEB Staff[10] and VECC[11] submit that both the Bucket Truck and Recloser ICM Projects have met the OEB's tests of Need, Materiality and Prudence, subject to the PILs and Capital Cost Allowance ("CCA") smoothing issue raised by OEB Staff and discussed below. In addition, the record in this proceeding demonstrates the approval of the ICM Projects is supported by E.L.K. Energy's customers. The utility hosted a Town Hall meeting in Essex, Ontario on November 13, 2023; providing customers the opportunity to engage directly with E.L.K. Energy regarding reliability and power needs in the future.[12] E.L.K. Energy received a positive response from customers, resulting in several letters of comment from residents served by E.L.K. Energy,[13] in addition to a letter of support from The Harrow & Colchester South Chamber of Commerce[14], all of which supported approval of the ICM Projects and funding.

E.L.K. Energy submits the OEB should approve the ICM Projects as filed. In the alternative, E.L.K. Energy submits that the OEB should approve the ICM projects subject to the implementation of the CCA smoothing mechanism proposed by E.L.K. Energy below.

PILs Issue & CCA Smoothing

The following are E.L.K. Energy's submissions with respect to the treatment of PILs relating to its ICM Projects and Z Factor Claims.

In summary, and as more fully detailed below:

1. The ICM is intended to be a funding mechanism for significant capital projects for which a utility required rate recovery in advance of its next regularly scheduled cost of service application.[15] Accepting OEB staff's submissions on the PILs issue would undermine this incentive by denying E.L.K. Energy incremental capital funding totalling $202,194 over the next three years. For a utility that already has negative earnings, this is a material and adverse financial disincentive that may undermine its ability to implement its longer term reliability improvement strategy as more fully detailed in the evidence.

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[10] Ibid., pp.14-15
[11] VECC Submission, pp.7-11
[12] EB-2023-0013 ELK_Letter of Comment_2024 IRM_20231122
[13] EB-2023-0013 ELK_Letter of Comment_2024 IRM_OEB_Residential_Support_20231122
[14] EB-2023-0013 SHarrow_Letter of Comment_20231101

[15] Report of the Board – New Policy Options for the Funding of Capital Investments: The Advanced Capital Module EB-2014-0219 at page 5.

2. The Halton Hills' 2019 ICM Decision is not relevant. As acknowledged by OEB Staff "[t]he negative grossed-up PILs adjustment was not brought up in the Halton Hill's 2019 ICM proceeding and therefore there was no discussion of the issue." Simply because Halton Hills did raise an issue should not preclude future applicants, like E.L.K. Energy, from doing so when the facts merit consideration by the OEB.

3. OEB Staff's hypothetical risk that the accumulated tax loss would "be lost" in E.L.K. Energy's next rebasing application is grossly overstated. The OEB has the authority to order, as part of its conditions of approval in this ICM application, that E.L.K. Energy be required to bring forward a proposal to address any tax losses as part of a true-up in its next cost of service rebasing application. This would ensure that a future OEB panel will have an opportunity to consider the ICM funding received, as well as any tax loss benefits associated with that funding, and whether it should accrue to ratepayers at that time.

4. E.L.K. Energy's proposed approach is consistent with the OEB's policy approach on other PILs anomalies in the ICM Model. Specifically: "The accelerated CCA should not be reflected in the ICM revenue requirement proposal associated with eligible assets/projects that are acquired after November 20, 2018. The OEB will assess the impact of the accelerated CCA on all capital investments at the time of rebasing to minimize the complexity of the review."[16]

5. Incorporating a 26.5% tax rate into the ICM model is grossly unfair to E.L.K. Energy. It effectively assumes that E.L.K. Energy will receive cash from the CRA in the amount of $67,397 in the 2024 test year, and each year thereafter. In reality, no cash will flow to E.L.K. Energy in the test year due to its forecast of ongoing losses. In fact, E.L.K. Energy may not realize on these tax losses for years to come. As noted above, any risk of "unfair" treatment to ratepayers is overstated and can be addressed through a condition on this ICM order.

6. OEB Staff's references to E.L.K. Energy's ROE performance between 2017-2021 is not relevant to the Application and is an express violation of the principle of no retroactive ratemaking.[17] The relevant means test when considering ICM funding is: "If the achieved regulated ROE <u>for the most recently completed fiscal year</u> exceeds 300 basis points above the deemed ROE embedded in the distributor's rates, that distributor does not qualify for funding for an incremental capital project." The evidence is that E.L.K.'s 2022 ROE was -1.97%. OEB Staff acknowledges that E.L.K. Energy has met the means test for ICM eligibility.

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[16] Ontario Energy Board Filing Requirements For Electricity Distribution Rate Applications - 2023 Edition for 2024 Rate Applications, Chapter 3 Incentive Rate-Setting Applications: page 30

[17] *Union Gas Limited v. Ontario Energy Board,* 2015 ONCA 453, para. 82 which provides: "*It is well established that an economic regulatory tribunal, such as the Board, operating under a positive approval scheme of ratemaking must exercise its rate-making authority on a prospective basis. Generally speaking, absent express statutory authorization, such a regulator may not exercise its rate-making authority retroactively or retrospectively.*"

E.L.K. Energy highlights for the OEB the importance of this issue and its impacts on E.L.K. Energy's financial and cash flow positions, having achieved negative ROE in 2022 and now entering a much-needed period of revitalization. OEB Staff concerns appear to focus on the ICM application resulting in a tax benefit to E.L.K. Energy which is not shared with customers. However, for clarity, E.L.K. Energy's 2022 Cost of Service[18] did not include any PILs amounts; E.L.K. Energy customers are currently not paying PILs in rates.

E.L.K. Energy believes consideration and relief on this issue is warranted when taking into account Section 1(1)2 of the *Ontario Energy Board Act, 1998*, which assigns the OEB the objective to "facilitate the maintenance of a financially viable electricity industry." As VECC made no submissions regarding E.L.K. Energy's proposed PILs treatment, these submissions respond entirely to those of OEB Staff.

While E.L.K. Energy disagrees with and refutes the arguments of OEB Staff against PILs treatment which responds to the utility's unique situation, E.L.K. Energy appreciates OEB Staff's suggestion that the utility propose a CCA smoothing mechanism to address the issue. E.L.K. Energy has proposed such a mechanism, which effectively responds to OEB Staff's concerns while meeting E.L.K. Energy's funding needs and maintaining financial viability.

Background

E.L.K. Energy's ICM Projects include two bucket trucks and six reclosing switches. As CCA Class 10 investments, the bucket trucks in particular have a high CCA rate of 30%. In E.L.K. Energy's pre-filed evidence, the utility stated the following with respect to the treatment of PILs within the OEB's ICM Model for the purpose of determining incremental funding for the ICM Projects:

> …E.L.K. is entering a period of revitalization in which capital expenditures above its historical trends are planned for. E.L.K. does not anticipate a reversal of the trend in which CCA deductions outstrip Net Income before Taxes and require the payment of PILs amounts. Further, E.L.K. notes its 2022 Regulated ROE was (1.97%); a trend which E.L.K. also expects to persist in the immediate future as it makes necessary investments to revitalize.
>
> The above said, it is inappropriate for E.L.K. to be subject to a negative PILs adjustment to the incremental revenue requirement resulting from its ICM requests in this case. The premise of negative ICM PILs adjustments are that these amounts will be netted out from actual PILs paid, leaving the utility in a net-neutral position. E.L.K. has no PILs amounts for such an adjustment to impact, and thus would simply lose recovery of a significant proportion of the incremental revenue requirement otherwise resulting from any approved ICM amounts; approximately half of incremental revenue requirement in fact.[19]

[18] EB-2021-0016
[19] E.L.K. Energy 2024 IRM Application, Appendix B – ICM Application, p.31

In the course of discovery, OEB Staff questioned E.L.K. Energy's proposed treatment of PILs in the ICM Model; soliciting further explanation, and calculation of ICM funding in a scenario where the full negative PILs adjustment was incorporated into ICM rate riders. E.L.K. Energy's response to these questions, included the following:

> E.L.K. Energy posted a significant tax loss of nearly $1 million for the year ended on December 31, 2022, and anticipates further tax losses in excess of $4 million from 2023 through 2026.
>
> It is in light of these tax losses (past, present and future) that E.L.K. Energy entered an effective tax rate of 0% in the OEB's ICM model to negate the impact of PILs on ICM funding. E.L.K. Energy notes that in a Cost of Service application the OEB's PILs model cannot generate PILs adjustments in rates that are below a value of $0, even where taxable income is below a value of $0. …
>
> …
>
> The effect of [implementing a 26.5% effective tax rate in the ICM model] is to reduce incremental revenue requirement by 51%;[20] from $138,591 to $71,193. Under this scenario, actual depreciation, deemed interest and return on equity associated with the ICM projects will continue to total $138,591 regardless of ICM funding approved, with no offsetting reduction to PILs costs as articulated in a) above.[21]

OEB Staff expressed concern regarding E.L.K. Energy's treatment of PILs in the ICM model within its Submission, listing four points of argument[22] which E.L.K. Energy responds to sequentially below.

Despite OEB Staff's views regarding E.L.K. Energy's proposed treatment of PILs, OEB Staff expressed a clear understanding of the urgency and importance of E.L.K. Energy's circumstances, stating that it "acknowledges E.L.K.'s concern of applying the current tax rate in the ICM model resulting in a negative gross-up PILs amount, thereby significantly reducing the ICM revenue requirements in this application."[23] Though advocating against E.L.K. Energy's proposal to ensure required levels of ICM funding are received, OEB Staff also expressed its concerns regarding E.L.K. Energy's most recent 2022 Return on Equity ("ROE") of negative 1.97%, encouraging "E.L.K. to take proactive steps to address this."[24]

Of note, the amount in question is not the difference between an ICM model with and without the negative PILs amount (i.e. $67,398), as the proposed ICM rate riders will be in place for rate years 2024, 2025 and 2026. A total 3-year reduction to ICM funding of $202,194 is a material amount for a utility of

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[20] In the course of preparing Reply Submission, E.L.K. Energy identified a typographical error relating to this figure. If required to incorporate an effective tax rate of 26.5% in the ICM Model, the resulting ICM funding would be 51% of the requested funding (as opposed to a 51% reduction to the proposed funding). As such, the change in effective tax rate would result in a 49% reduction to ICM funding

[21] E.L.K. Energy Response to OEB Staff 8

[22] OEB Staff Submission, p. 18

[23] Ibid.

[24] Ibid., p.14

E.L.K. Energy's size, and would significantly hamper efforts to improve financial health while revitalizing the utility.

OEB Staff's concern is disconnected from its submissions that E.L.K. Energy should receive ICM funding which is less than the cost of depreciation, deemed interest and return on equity for important investments OEB Staff submits meet the need, materiality and prudence tests. Clearly, implementation of OEB Staff's PILs recommendation would make E.L.K. Energy's ROE worse. While E.L.K. Energy disagrees with and responds to the 4-part submission of OEB Staff regarding PILs treatment, E.L.K. Energy acknowledges that OEB Staff correctly identified the crux of this issue as the differential between accounting depreciation and CCA, and invited E.L.K. Energy to submit a proposal for a CCA smoothing mechanism which addresses the issue.[25] E.L.K. Energy has provided such a proposal below, and submits that it is responsive to OEB Staff's comments and an effective means to address E.L.K. Energy's unique circumstances.

Filing Requirements

OEB Staff's submission asserts that because the Filing Requirements for ICM applications call for use of the current effective tax rate in the ICM model, E.L.K. Energy's proposal for an exception to this rule should be rejected.

In E.L.K. Energy's submission, this argument ignores the OEB's demonstrated willingness to implement exceptions to established ICM policy where the evidence of an individual case warrants exception and unique treatment. By way of example, in Elexicon Energy's 2025 ICM Application,[26] the OEB approved[27] the use of the OEB's 2023 Inflation Factor rather than the most recent available 2024 Inflation Factor, based on the specific circumstances of that case.

Though the circumstances differ, E.L.K. Energy's application is similarly seeking the OEB's approval of an exception based on its unique situation. E.L.K. Energy submits that the circumstances of this case are unquestionably unique, and warrant OEB consideration. Of particular note:

- E.L.K. Energy is in a position of negative ROE, in which cashflow in addition to cost recovery are incredibly important to maintain financial viability;
- The utility has only recently entered a period of revitalization, in which significant capital investments (and thus funding) are required to maintain a safe and reliable system. A material ICM funding reduction of $202,194 stands to slow down projected investment in much needed revitalization;
- Absent the ICM Projects, E.L.K. Energy nonetheless anticipates accruing a significant tax loss carry forward as it approaches next rebasing;

[25] Ibid., p.21
[26] EB-2022-0024
[27] https://www.rds.oeb.ca/CMWebDrawer/Record/808601/File/document

- The size of the ICM funding reduction resulting from a standard negative PILs adjustment is nearly half of the ICM funding request, as further discussed below; and,
- Implementation of the negative PILs adjustment creates the potential for double counting of the CCA tax benefit to ratepayers. First, ratepayers would receive the upfront benefit of reduced ICM funding in rates resulting from a negative PILs adjustment which yields no corresponding savings for the utility. Second, the actual tax-loss carryforwards resulting from the actual tax losses driven by the ICM Projects would likely be included in E.L.K. Energy's next rebasing, again reducing rates by offsetting or eliminating ratepayer payment of PILs amounts.

Halton Hills 2019 ICM Decision

E.L.K. Energy disagrees with OEB Staff's submissions relying on the OEB's Decision in Halton Hills Hydro Inc.'s ("Halton Hills") 2019 ICM application (EB-2018-0328) as justification to deny E.L.K. Energy's request, for 3 primary reasons.

First, the financial viability of Halton Hills was not in question at the time the OEB heard its ICM application. As noted above, E.L.K. Energy had negative ROE of 1.97% in 2022, and OEB Staff itself suggests E.L.K. Energy should take pro-active steps to address this issue. Conversely, Halton Hills had an Achieved ROE in 2019 of 4.24%.[28] More so, to the degree cash flow was of vital important to Halton Hills in 2019 as it relates to the negative PILs, it stands to reason Halton Hills would have raised this issue to the OEB. As noted by OEB Staff, "The negative grossed-up PILs adjustment was not brought up in Halton Hill's 2019 ICM proceeding and therefore there was no discussion of the issue."[29]

Second, the quantum of negative PILs adjustment implemented in EB-2018-0328 was orders of magnitude smaller than those contemplated in this case relative to the size of ICM Funding requested, as shown in the table below. E.L.K. Energy submits it would be inappropriate to characterize the impacts of these two negative PILs adjustments as remotely comparable.

	Halton Hills 2019	E.L.K. Energy 2024
PILs Adjustment	-$ 152,818	-$ 67,397
ICM Funding (excl. PILs Adj.)	$ 1,850,903	$ 138,591
PILs Adj. vs. ICM Funding	**8%**	**49%**

Finally, as stated in evidence E.L.K. Energy is seeking OEB approval of its request on an exception basis to reflect the unique circumstances of E.L.K. Energy in this application, and the experience of Halton Hills in

[28] EB-2020-0026, Exhibit 5 – Cost of Capital, p.5
[29] OEB Staff Submission, p.19

EB-2018-0328 does not fetter the OEB Panel in this proceeding in its ability to make decisions based on the facts at hand. The quantum of negative PILs adjustment contemplated, the reality that the negative PILs adjustment was never raised in EB-2018-0328, and E.L.K. Energy's demonstrated financial viability concerns appealing to Section 1(1)2 of the *Ontario Energy Board Act, 1998*, all distinguish this case from the Halton Hills example raised by OEB Staff.

E.L.K. Energy submits the comparison between Halton Hills in 2019 and E.L.K. Energy in 2024 is mistaken, and the OEB should place no weight on such a comparison in rendering its decision in this proceeding.

Realization of Tax Benefits

OEB Staff suggests in its submission that by utilizing a 0% effective tax rate in the ICM model, and thus neutralizing the impact of negative PILs on ICM riders and revenues, the utility may ultimately lose actual tax benefits resulting from the CCA associated with the ICM projects. E.L.K. acknowledges this concern, and has prepared its CCA smoothing proposal in a manner that fully addresses these concerns.

Benefit Sharing with Ratepayers

OEB Staff's submission suggests that ratepayers did not share in the benefits of E.L.K. Energy's higher-than-deemed ROE in past years. E.L.K. Energy submits that this is a mischaracterization which ignores key realities of E.L.K. Energy's circumstances in the past and present.

As noted in evidence, E.L.K. Energy is entering a period of revitalization, in which significant investments are required to restore and modernize E.L.K. Energy's infrastructure and business. To some degree, E.L.K. Energy's past years' higher-than-deemed ROE was a reflection of a frugal approach to system and business investment. One result of this, was E.L.K. Energy's shareholders receiving the benefit of higher-than-deemed ROE. However, to suggest that "ratepayers haven't shared the benefits"[30] of E.L.K. Energy's prior investment approach is incorrect.

E.L.K. Energy's ratepayers received the benefit of extremely low distribution rates during the period in which higher-than-deemed ROE was achieved by the utility. Relying on the OEB's publicly available and published Open Data (formerly presented in the OEB's Electricity Distributor Yearbook), the average distribution revenue per customer in 2022 amongst Ontario LDC's was $587. The highest distribution revenue per customer was $2,146, while the lowest was $298;[31]. E.L.K. Energy's distribution revenue per

[30] OEB Staff Submission, p.18
[31] Calculated as distribution revenue divided by customer count. The average distribution revenue per customer presented is a simple average of the distribution revenue per customer applicable to each distributor in Ontario

customer of $298 is quite literally the lowest in the Province by a reasonable margin, at approximately half the average of distributors in Ontario. Similarly, as of May 2023, E.L.K. Energy had the lowest residential distribution charge and fourth lowest distribution charge for General Service less than 50 kW Rate Class of any LDC in Ontario[32].

Historical investment approaches have yielded significant benefits for ratepayers in the form of lower distribution rates, with accompanying benefits for E.L.K. Energy's shareholders through higher-than-deemed ROE. This historical approach also resulted in approval of a Revenue Sufficiency in E.L.K. Energy's 2022 Cost of Service,[33] reducing distribution rates further for customers and setting cost-based rates which did not include any PILs amounts. Today however, E.L.K. Energy has refreshed leadership at the Board of Directors level and entered into a Management Services Agreement with Entegrus Inc. A significant shift in management practices has been identified as necessary, resulting in E.L.K. Energy pro-actively accepting reductions to its earnings (to the point of negative earnings) in order to ensure the long-term safe and reliable delivery of electricity to its customers. Both shareholders and ratepayers received benefits as a result of E.L.K. Energy's past investment practices, however both must now financially contribute to ensure the system is revitalized in the near-term. As such, there is no unjust treatment of ratepayers resulting from E.L.K. Energy's ICM and Z Factor PILs proposals in this application.

Even were the OEB to set all of the above aside, E.L.K. Energy submits that to reject just and reasonable rate requests in 2024 based on earnings achieved in 2021 and earlier amounts to retroactive ratemaking, and is contrary to case law.[34] Setting rates in 2024 in a manner which consciously seeks to recoup earnings from past years which are perceived to be in excess is directly contradictory to this core regulatory principle.

CCA Smoothing Proposal

OEB Staff suggested in its Submission that E.L.K. Energy comment on a CCA smoothing mechanism in its Reply Submission. OEB Staff further articulated the core challenge in this unique circumstance, stating:

> "The concern arises due to the difference in calculating the CCA on a declining basis and the accounting amortization expense on a straight line basis. The gap between the accounting depreciation and the CCA is most significant in the first year when the CCA is deducted the

[32] OEB Open Data Current Electricity Rates (Residential Rate Class) : https://www.oeb.ca/open-data/current-electricity-rates-residential-rate-class & OEB Open Data Current Electricity Rates (General Service < 50 kW Rate Class) https://www.oeb.ca/open-data/current-electricity-rates-general-service-50-kw-rate-class

[33] EB-2021-0016

[34] See citations in Footnote 16 & Louisiana Power & Light Co. v. Louisiana Pub. Serv. Comm'n, 377 So. 2d 1023, 1029 (La. 1979); State ex rel. Util. Consumers Council v. Public Serv. Comm'n, 585 S.W.2d 41, 59 (Mo. 1979); State ex rel. Util. Comm'n v. Edmisten, 232 S.E.2d 184, 194-95 (N.C. 1977); Narragansett Elec. Co. v. Burke, Nos. 84-73-M.P., 84-232-M.P. & 84-342-M.P. at *4 (R.I. Mar. 11, 1986) (LEXIS, RI library, RI file)

most in the taxable income calculation. This gap is further magnified when the CCA rate is much higher than the accounting amortization rate."[35]

OEB Staff's submissions regarding this core challenge are correct, as articulated in the table below comparing the accounting depreciation rates and CCA rates of the bucket truck and recloser ICM projects, respectively:

ICM Project	Accounting Depreciation (%)	CCA (%)	Accounting Depreciation ($)	CCA ($)[36]
Bucket Trucks (CCA Class 10)	6.67%	30%	$ 58,994	$ 265,472
Reclosing Switches (CCA Class 47)	2.50%	8%	$ 12,126	$ 38,802

The above noted gap between accounting depreciation and CCA claimed at its maximum results in the ICM Projects, in isolation of all other utility financials, generating negative taxable income and a resulting negative PILs adjustment. Fortunately, OEB Staff's suggestion to utilize CCA as a means to smooth this discrepancy provides the opportunity for E.L.K. Energy to collect revenues which are equal to the cost of depreciation/amortization, deemed interest, and return on equity, without sacrificing the tax benefits associated with the ICM Projects' CCA, as outlined below.

Though it is common practice for most businesses and individuals in Canada is to deduct the full amount of eligible CCA each year from taxable income, CCA is in fact an optional tax deduction. To the degree a person or business chooses to, it may deduct all, some, or none of the eligible CCA associated with a depreciable asset in a given tax year. To the degree CCA deducted is less than the maximum eligible CCA, these amounts will remain in the entity's Undepreciated Capital Cost ("UCC") balance to be claimed as a tax deduction in future years.

As a CCA smoothing mechanism, E.L.K. Energy proposes to deduct for income tax purposes the exact amount of CCA relating to the ICM Projects required to yield taxable income of $0, resulting in PILs associated with the ICM Projects of $0. To implement this smoothing, total CCA claimed against the ICM Projects must be equal to the total annual accounting depreciation of the ICM Projects, plus the total return on equity associated with the ICM Projects. Mathematically, E.L.K. Energy proposes to establish CCA claims for each ICM Project by adding the accounting depreciation of each ICM Project to a pro-rated portion of the total return on equity associated with the ICM Projects, as calculated below:

[35] OEB Staff Submission, p.21
[36] Year 1 CCA when excluding the Half-Year Rule for purposes of ICM Model

	Accounting Depreciation	Proportion of Total Accounting Depreciation	Allocation of Return on Equity	Proposed CCA Claim	Maximum CCA Claim	Difference: Proposed vs. Maximum CCA
200-42 Bucket Truck	$ 27,079	38%	$ 17,600	$ 44,679	$ 121,857	$ 77,178
400-46 Bucket Truck	$ 31,914	45%	$ 20,742	$ 52,657	$ 143,615	$ 90,958
6x Reclosing Switches	$ 12,126	17%	$ 7,881	$ 20,006	$ 38,802	$ 18,796
Total	**$ 71,119**		**$ 46,223**	**$ 117,342**	**$ 304,274**	**$ 186,932**

By claiming a smaller amount of CCA than the maximum eligible CCA, E.L.K. Energy will preserve the UCC associated with the assets to be claimed in future years; creating the opportunity to reduce or avoid PILs costs in rates in future years. Taken together, E.L.K. Energy's CCA smoothing proposal ensures E.L.K. Energy receives much needed cost recovery and cashflow, while simultaneously ensuring UCC is preserved for the future benefit of the utility and ratepayers. The proposed CCA Claims articulated in the table above have been included in a revised version of E.L.K. Energy's ICM Model, as filed concurrent with this Reply Submission.

With respect to OEB Order(s) enacting the proposed CCA smoothing mechanism, E.L.K. Energy proposes some version of the following, in addition to any other Orders the OEB deems necessary:

1. An Order requiring E.L.K. Energy to submit CCA deductions associated with the combined ICM Projects in its tax returns which are equal to accounting depreciation plus return on equity, up to the effective date of its next rebasing; and,
2. An Order to report on historical CCA and UCC associated with the combined ICM Projects as part of its next rebasing application.

E.L.K. Energy has proposed the same treatment be applied to its Z Factor capital claims for the same reasons articulated above with respect to the ICM Projects for consistency, and has incorporated this approach into the revised Z Factor claims and rate riders attached to this Reply Submission.

Conclusion

Subject to the adjustments proposed in this Reply Submission and its accompanying attachments, E.L.K. Energy submits the OEB should approve its IRM, ICM and Z Factor application as filed.

All of which is respectfully submitted.