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

BY EMAIL

September 27, 2024

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
Essex Powerlines Corporation
2025 Cost of Service Application
OEB File Number: EB-2024-0022/EB-2024-0096

Please find attached OEB staff's submission in the above referenced proceeding.

Yours truly,

Original Signed By

Amber Goher
Digitally signed by Amber Goher
Date: 2024.09.27 12:14:31 -04'00'

Amber Goher
Advisor – Electricity Distribution Rates I

Encl.

cc: All parties in EB-2024-0022/EB-2024-0096

ONTARIO ENERGY BOARD

OEB Staff Submission

Essex Powerlines Corporation

Cost of Service Application

EB-2024-0022/EB-2024-0096

September 27, 2024

1. Introduction

This is OEB staff's submission on a partial settlement proposal filed by Essex Powerlines Corporation (Essex Powerlines) related to its application for January 1, 2025 electricity distribution rates (Application). The settlement proposal represents a partial settlement on all issues except issues 7.4 and 7.5 on the OEB-approved issues list.[1]

The partial settlement proposal was arrived at during a settlement conference held from August 7, 2024 to August 9, 2024. The parties to the settlement proposal include Essex Powerlines and 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 partial settlement proposal.

If the partial settlement proposal is approved, a typical residential customer with a monthly consumption of 750 kWh would see a total bill[2] decrease of $9.09 or (6.62%) per month.

This submission reflects observations that arise from OEB staff's review of the evidence and the partial settlement proposal. It is intended to assist the OEB in deciding upon Essex Powerlines' Application and the partial settlement Proposal.

[1] EB-2024-0022/EB-2024-0096: OEB Approved Issues List
[2] 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 are 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 Essex Powerlines.

OEB staff's position was developed in consideration of the objectives of the *Renewed Regulatory Framework*[3] (RRF), the *Handbook for Utility Rate Applications*[4], 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.[5]

- 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

[3] Report of the Board – *Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach*, October 18, 2012
[4] *Handbook for Utility Rate Applications*, October 13, 2016
[5] 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?

The Parties settled capital expenditures and rate base amounts with the exception of the Distribution System Operator (DSO) PowerShare-related costs. The Parties agreed to the determination of the 2025 capital additions related to the DSO PowerShare related costs by way of a written hearing process, which is outlined in the settlement proposal.[6] OEB staff support the proposed approach to addressing this item.

OEB staff supports the proposed capital expenditures and in-service additions as outlined in the partial settlement proposal, which exclude the DSO PowerShare-related amounts. Through settlement, the Parties agreed to 2024 in-service additions of $7,357k, a reduction of $1,950k as shown in Table 1.1A. Of the reductions, $700k for the purchase of Hydro One Networks Inc. (HONI) assets is to be recorded in a DVA outlined in Issue 6.

The parties also agreed to reduce 2025 capital work by $1,599k for a total capex of $8,236k. Of the reductions, $384k is for the purchase of HONI assets is to be recorded in a Deferral and Variance Account (DVA) outlined in Issue 6, and $975k is to level the yearly expenditures over the rate period.

Adjustments to capital expenditures and in-service additions are made on an envelope basis.

OEB staff submits the proposed in-service additions budget is sufficient for Essex Powerlines to continue to operate its system reliably.

1.2 Are the proposed rate base and depreciation amounts appropriate?

OEB staff considers the 2025 rate base and depreciation amounts reasonable. The 2025 rate base and depreciation amounts have been calculated on the basis agreed to by the Parties.

The proposed 2024 rate base is $80.6M, a $2.9M (3.4%) reduction from the amount included in the Application.[7] The reduced rate base agreed to by the Parties is due to reductions in capital additions, OM&A, cost of power and working capital allowance. The

[6] Settlement Proposal, p. 17
[7] Ibid, pp. 17-19

proposed 2025 depreciation amount is $4.0M as shown in Table 1.2A.

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 2025 OM&A expenses reasonable.

Essex Powerlines proposed total OM&A expenses of $10.3M for the 2025 Test Year in the Application, an increase of 42.3% (or 5.2% compounded annually) compared to the 2018 OEB-approved amount of $7.2M. Essex Powerlines stated that the OM&A cost increases have been driven by inflation, salaries and benefits, increased customer billing and collecting costs, higher levels of general administration (IT software, hardware and cybersecurity) and materials costs.[8]

In 2018, Essex Powerlines achieved an efficiency assessment of 2 in Pacific Economics Group's (PEG) Benchmarking report to the OEB. In 2023, Essex Powerlines achieved Group 1 ranking, the most efficient group of Ontario Electricity Distributors.[9] As stated in the partial settlement proposal, Essex Powerlines is expected to be in Group 2 (the second most efficient group) productivity rating during all of its IRM term.

Through settlement, the Parties have agreed to an envelope reduction of $675k to Essex Powerlines proposed 2025 OM&A expenses. The revised 2025 OM&A spending represents an increase of 23% (or 3% compounded annually) compared to the 2018 actual OM&A spending.

In the context of the overall settlement proposal, OEB staff submits that the envelope reduction of $675k in OM&A is reasonable. OEB staff further notes that the settled OM&A envelope should ensure that Essex Powerlines 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

[8] Exhibit 4, p. 18-19
[9] Exhibit 1, p. 65

Tables 3.1A and 3.1B of the settlement proposal on the basis that the cost of capital calculation has been determined in accordance with OEB policies and practices.

Essex Powerlines proposed to use the OEB deemed capital structure of 4% short term debt, 56% long term debt, and 40% equity. The Parties agreed that Essex Powerlines shall update the cost of short term debt and the return on equity once the OEB releases the 2025 “Cost of Capital Parameter Updates”, and Essex Powerlines will file an updated Draft Rate Order for approval, along with the updated models, once the 2025 cost of capital parameters are issued.

As part of the agreements reached through the settlement process, Essex Powerlines agreed to update, as part of the Draft Rate Order Process, the interest rate for the December 28, 2024 loan with the lower of: (a) the deemed long-term debt rate issued by the OEB for the 2025 Cost of Capital Parameters; or (b) the quoted rate from TD Bank for a 20 year amortization loan at the time of the Draft Rate Order process. In the interim, Essex Powerlines used the most recent forecast interest rate obtained from TD Bank for the December 28, 2024 loan.

OEB staff notes that Essex Powerlines confirmed that it will comply with the applicable cost of capital parameters resulting from the OEB’s generic proceeding on Cost of Capital and Other Matters, EB-2024-0063.[10]

OEB staff has no other comments on the cost of capital or capital structure and supports the update through the Draft Rate Order process.

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

OEB staff does not take issue with the forecast PILs expense of $11,856 as agreed to by the Parties. The PILs also reflected a five-year smoothing method for capital cost allowance (CCA) to address the phase-out of the accelerated CCA rules[11] in 2028.

The smoothing adjustment added to test year regulatory net income before taxes of $74,688 as set out under Issue 3.2 of the settlement proposal is calculated based on 2025 capital additions. Without the smoothing adjustment, the PILs expense would be nil, as the regulatory net income would have been negative $31k

Regarding the CCA smoothing method, OEB staff notes that 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*, the OEB stated that it may consider a smoothing mechanism to address any timing differences that could lead to volatility in tax deductions over the rate-setting term. OEB staff also notes that CCA smoothing proposals have been previously accepted by the OEB in settlement proposals of other

[10] Interrogatory Response, 5-Staff-53
[11] Accelerated CCA was introduced through the Accelerated Investment Incentive program, to provide for a first-year increase in CCA deductions on eligible capital assets acquired after November 20, 2018.

proceedings.[12] In OEB staff's view, the agreed-upon smoothing adjustment calculation in Essex Powerlines' partial settlement proposal is one of the appropriate methods to address the phase-out of accelerated CCA. Therefore, OEB staff does not take issue with Essex Powerlines' smoothing adjustment calculation.

Additional details of Account 1592, Sub-account CCA Changes are discussed under Issue 6.1.

3.3 Is the proposed Other Revenue forecast appropriate?

OEB Staff has no concerns with the proposed Other Revenue forecast. Through interrogatories and the pre-settlement clarification questions, Essex Powerlines updated the 2025 Test Year other revenue forecast to $1.16M, an increase of $52.9k compared to $1.11M included in the Application (Table 3.3A of the settlement proposal).

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 proposed by the Parties for this element of the application.

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 $18.4M and a base revenue requirement of $17.3M.[13] These values reflect a reduction in the 2025 OM&A expenditures of $675k, respectively, compared to the Application. The values also reflect changes to rate base, revenue offsets, depreciation, working capital allowance and PILs. Table 3.5A (p.45) of the partial settlement proposal shows the change in revenue requirement between the Application, interrogatories, and the settlement proposal.

Issue 4: Load Forecast

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

[12] Brantford Power Inc. 2022 Cost of Service Decision and Rate Order, EB-2021-0009, November 25, 2021, PUC Distribution Inc. 2023 Cost of Service Decision and Rate Order, EB-2022-0058, April 6, 2023
[13] Settlement Proposal, Table B, p.6

appropriate?

The parties agreed to the load forecast subject to an update to the CDM Framework tab of the model.

OEB staff supports the proposed consumption, demand and customer forecasts of 591 GWh, 810 MW, and 34,922 respectively (Table 4.1A of the settlement proposal and the included Load Forecast model). Relative to the Application, this reflects a decrease of 4 GWh in the Residential class, partially offset by an increase of 3 GWh in other rate classes. It also reflects an increase of 13 MW for demand and a decrease of 36 customers.

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 to two changes to the cost allocation proposed by Essex Powerlines.

1. The meter reading expense for the Embedded Distributor rate class should be calculated based on the number of bills per customer. This change brings it into consistency with the approach used for all other metered rate classes.
2. The revenue to cost ratios would be adjusted such that the Sentinel Lighting revenue-to-cost is increased to 80% (the lower end of the target range) over 3 years. The GS 50 – 4,999 kW, USL, and Embedded Distributor revenue-to-cost ratios are reduced to 120.46% in 2025 and reaching 120% (the top end of the target range) in 2027. These changes offset in 2026 and 2027. The resulting shortfall in 2025 is recovered by increasing the revenue-to-cost ratio for the Residential and Street Lighting rate classes to 94.17%.

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 Essex Powerlines' proposal for fixed / variable splits is appropriate.

OEB staff does not have any concerns with the proposed rate design, including the fixed/variable splits.

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

The parties agreed that Essex Powerlines would use 2023 load forecast data and 2023 actual wholesale volumes in the RTSR workform. OEB staff agrees that it is appropriate to use the same historic year for both wholesale and retail volumes. 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 total loss factor of 4.25% as shown in the settlement proposal. OEB staff notes that this reflects an increase from the current approved 3.55%. The proposed Distribution loss factor is 1.65% which remains below 5%.

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

The Parties agreed with Essex Powerlines' proposed Specific Service Charges and Retail Service Charges which are unchanged from previous approved rates. OEB staff have no concerns with the proposed Specific Service Charges and Retail Service charges.

5.6 Are rate mitigation proposals required and appropriate?

The Parties agreed that mitigation was only required for the Sentinel Lighting rate class, which was mitigated by spreading the increase in the revenue-to-cost ratio over 3 years, as detailed in issue 5.1.

OEB staff has no concerns with the agreed-upon rate 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 agreement reached by the Parties relating to DVAs.

The Parties agreed to the disposition of the following DVA balances as of December 31, 2023, and forecasted interest through to December 31, 2024, over a one-year disposition period.

- Group 1 DVAs of a total credit balance of $132,275
- Group 2 DVAs of a total credit balance of $2,734,424

As part of the settlement proposal, the Parties agreed to the following adjustments[14]:

a) Essex Powerlines will forecast the Pole Attachment Revenue Variance Account balance to December 31, 2024, and dispose of the account on a final basis, thereby allowing Essex Powerlines to close the account.
b) Essex Powerlines agreed to close out Account 1535-Smart Grid OM&A Deferral Account and will not seek recovery from ratepayers.

[14] Settlement Proposal, p.53

c) Essex Powerlines agreed to close out Account 1576 – Accounting Changes Under CGAAP Balance & Return Comp and will not seek recovery from ratepayers.
d) Essex Powerlines agreed to forecast the Accelerated CCA sub-account of Account 1592 balance to December 31, 2024, and disontinue the account after the final disposition of the balance.

OEB staff has no issue with the proposed discontinuation of the Group 2 accounts.

Account 1592 – PILs and Tax Variances, Sub-account CCA Changes

Bill C-97 introduced the Accelerated Investment Incentive Program (AIIP), which provides for a first-year increase in 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 entitled *Accounting Direction Regarding Bill C-97 and Other Changes in Regulatory or Legislated Tax Rules for Capital Cost Allowance*, 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. The credit balance of $2,169,019 in sub-account CCA Changes of Account 1592 represents the full revenue requirement impact of the application of accelerated CCA as of December 31, 2024, including interest to December 31, 2024.

The parties also agreed that Account 1592 – PILs and Tax Variances, Sub-account CCA Changes subsequent to December 31, 2024, is to be discontinued. OEB staff agrees with this approach, given that Essex Powerlines has smoothed out the AIIP impact in its incentive period in this proceeding. Account 1592, Sub-account CCA Changes was established to track the impact of any differences that result from a change in the CCA rule used to determine the tax amount that underpins rates.[15]

As noted in the OEB's *Filing Requirements for Electricity Distribution Rate Applications*[16], 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. In OEB staff's view, a smoothing adjustment intends to address the change in CCA rules resulting from the phase-out of accelerated CCA upfront in the current application, instead of capturing the impact of those rule changes as they occur during the IRM period. Therefore, the 1592 sub-account would no longer be needed because the AIIP is expected to be phased out starting in 2024 and fully phased out in 2028.

[15] Account 1592, Sub-account CCA Changes was established in the OEB's letter Accounting Direction Regarding Bill C-97 and Other Changes in Regulatory or Legislated Tax Rules for Capital Cost Allowance, July 25, 2019
[16] OEB-Filing-Reqs-Chapter-2-2023-Clean-20221215.pdf

New DVA – Account 1508, Sub-Account HONI Asset Purchases Deferral Account

For the purpose of settlement, the Parties agreed to remove the forecasted capital expenditures for purchases of HONI distribution assets from Essex Powerlines' budget. The partial settlement proposal states that Essex Powerlineshas not yet executed agreements for these purchases with HONI. Additionally, such transaction may require OEB approval under section(s) 81 and/or 86 of the Ontario Energy Board Act.[17]The Parties agreed to the establishment of a new deferral and variance account (DVA), Account 1508 – Sub-Account HONI Asset Purchases Deferral Account and sub-accounts to capture the revenue requirement associated with the purchase of existing assets from HONI by Essex Powerlines. Additional details distribution assets purchase are discussed under Issue 1.1.

OEB staff has no issue with the proposed new DVA and the sub-accounts, given that the agreements with HONI have not yet been executed and the potential purchases will occur over multiple years. OEB staff is of the view that, by recording the revenue requirement associated with the HONI asset purchases in the new DVA, Essex Powerlines will be kept whole while ensuring customers are not prematurely burdened with costs for purchases that may be subject to change or delay.

OEB staff notes that Essex Powerlines addressed the causation, materiality, and prudence criteria for establishing new accounts in the settlement proposal[18]. Further, OEB staff reviewed the draft accounting order attached to the settlement proposal and has no concerns.

Issue 7: Other

7.1 Is the proposed effective date appropriate?

OEB staff supports the partial settlement proposal with respect to Essex Powerlines' requested effective date of January 1, 2025.

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

OEB staff supports the Parties' view that Essex Powerlines has responded appropriately to all previous OEB directions.

7.3 Is Essex Powerlines' z-factor claim for recovery of costs related to a February

[17] Settlement Proposal, p.15
[18] Settlement Proposal, p.54

2023 ice storm appropriate?

Essex Powerlines proposed, and the Parties agreed that Essex Powerlines' z-factor claim for recovery of costs related to a February 2023 ice storm is appropriate. Essex Powerlines proposed to recover $209k in incremental operating costs which exceeds its materiality threshold through a fixed rate rider over a 12-month period starting January 1, 2025.

OEB staff has no concerns with the proposed recovery of the $209k z-factor amount using a 12-month fixed rate rider.

~All of which is respectfully submitted~