KITCHENER WILMOT HYDRO INC.
P.O. BOX 9010
301 VICTORIA STREET SOUTH
KITCHENER, ONTARIO
N2G 4L2

Jerry Van Ooteghem
President & CEO
Tel: (519) 745-4771
Fax: (519) 571-9338

February 6, 2014

BY RESS & COURIER

Ms. Kirsten Walli, Board Secretary
Ontario Energy Board
2300 Yonge Street, 26th Floor, P.O. Box 2319
TORONTO, ON   M4P 1E4

Re: Board File No. EB-2013-0147
Kitchener-Wilmot Hydro Inc. – Reply Submission

Dear Ms. Walli:

At the conclusion of the Oral Hearing held on January 9, 2014 the Board issued a directive to KWHI to submit its Reply Submission to the Board and all registered Intervenors on or before February 6, 2014. KWHI now respectfully submits its Reply Submission.

A copy of this submission has been electronically filed through the Board's RESS system. The original has been couriered to the Board's offices.

Should you require any further information or clarification of any of the above, kindly contact the writer.

Respectfully submitted,

Original Signed by

J. Van Ooteghem, P.Eng.
President & CEO

cc All Intervenors

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EB-2013-0147

IN THE MATTER OF the *Ontario Energy Board Act,* 1998,being Schedule B to the *Energy Competition Act*, 1998, S.O. 1998,c.15;

AND IN THE MATTER OF an Application by Kitchener-Wilmot Hydro Inc. to the Ontario Energy Board for an Order or Orders approving or fixing just and reasonable rates and other service charges for electricity distribution to be effective January 1, 2014.

REPLY SUBMISSION OF KITCHENER-WILMOT HYDRO INC.

FILED FEBRUARY 6, 2014

INTRODUCTION

1. Kitchener-Wilmot Hydro Inc. ("KWHI") owns and operates the electricity distribution system in the City of Kitchener and the Township of Wilmot and serves approximately 90,500 customers.

2. On June 21, 2013, KWHI filed its Cost of Service Application for distribution rates effective January 1, 2014. Energy Probe, the School Energy Coalition ("SEC") and the Vulnerable Energy Consumers Coalition ("VECC") requested and were granted Intervenor status.

3. The evidence in this proceeding consists of the Application, Intervenor Interrogatories and KWHI's responses to same; questions provided to KWHI prior to the Technical Conference, a Technical Conference held on October 28, 2013 and Undertakings; a Partial Settlement Proposal; and an Oral Hearing held on January 9, 2014 with Undertakings. As mentioned by Mr. Van Ooteghem in his Evidence in Chief[1], KWHI may have run

[1] TR, Vol. 1, Page 19 lines 18-26

alternative scenarios for the purpose of responding to Interrogatories or Technical Conference questions but KWHI does not necessarily support these alternative approaches.

4. The Settlement Conference in this proceeding concluded on November 8, 2013 with a comprehensive Partial Settlement. The following issues are outstanding:

- Issue 2.2: Is the WCA for the Test Year appropriate?
- Issue 4.1: Is the overall OM&A forecast for the Test Year appropriate?

5. The following issue was shown as incomplete in so far as it relates to KWHI's WCA:

- Issue 1.1: – Has KWHI responded appropriately to all relevant Board directions from previous proceedings?

6. As discussed in the Settlement Proposal[2], the parties have agreed that the effective date of the rates arising out of the proposed agreement and the Board Decision on OM&A and WCA should be January 1, 2014. KWHI will calculate a rate rider for the remainder of the Test Year that will enable KWHI to refund/recover the difference between its incremental Board-approved revenue and its revenue at existing rates, for any months in 2014 in which its new rates are not in effect. KWHI will provide the appropriate calculation in conjunction with its Draft Rate Order following the Board's Decision in this proceeding. The Board's Decision on the Settlement Proposal is outstanding but KWHI understands that the Board will issue its Decision on the Settlement Proposal in conjunction with its Decision on the unsettled issues.

7. KWHI delivered its Argument-in-Chief pertaining to the outstanding issues orally on January 9, 2014 following the conclusion of the Oral Hearing. KWHI received submissions from Board staff, Energy Probe and VECC on January 23, 2014, and from SEC on January 30, 2014.

[2] Settlement Proposal, Page 5

8. Throughout this proceeding, KWHI has attempted to ensure that its evidence and responses to Interrogatories and Undertakings have been clear and that it has assisted the Board and parties in understanding both the Application and KWHI's positions on the outstanding issues.

9. KWHI repeats and relies upon the submissions in its Argument-in-Chief. KWHI offers the following submissions on the outstanding issues in reply to those of Board staff, Energy Probe, SEC and VECC.

ISSUE 1.1: HAS KWHI RESPONDED APPROPRIATELY TO ALL RELEVANT BOARD DIRECTIONS FROM PREVIOUS PROCEEDINGS?

10. In its Argument-in-Chief, KWHI stated that it did not conduct a lead/lag study nor did the Board direct it to do so in its Decision (EB-2009-0267)[3] on KWHI's 2010 rate application. In its Decision (EB-2009-0267), dated April 7, 2010, the Board wrote:

> *"...and that the Board may initiate a generic proceeding/consultation on determining a new working capital methodology in advance of KW Hydro's next cost of service filing. In such case, the Board expects that KW Hydro will participate in such a process…"*

In the same paragraph, the Board writes:

> *"The Board expects that KW Hydro will support its cash working capital allowance in its next rebasing application based on the outcomes of this Board-Led process **or** based on the Lead/Lag study that KW Hydro stated would individually undertake*." (Emphasis added).

Board Staff and Intervenor Submissions

11. Board staff noted that KWHI was not directed to do a lead/lag study. Board staff submits that KWHI's reliance on the updated default Working Capital Allowance (WCA) factor of 13% is reasonable.

[3] EB-2009-0267, page 27

12. Energy Probe submits that KWHI should have followed the Board's directive and filed a lead/lag study given that there was no generic proceeding/consultative in which the Board expected KWHI to participate.

13. SEC asserts that KWHI was directed to do a lead/lag study.

KWHI's Reply:

14. The April 12, 2012 Board letter, in which the Board updates the OEB Filing Requirements for Transmission and Distribution Applications, states:

> *"The Board has reviewed the approaches to the calculation of WCA and will not require distributors to file lead/lag studies for 2013 rates, unless they are required to do so as a result of a previous Board Decision."*

15. Consistent with the observation of Board staff, KWHI submits that it was not required to file a lead/lag study as a result of its previous Board Decision (EB-2009-0267)[4].

16. The Board letter that was issued on April 12, 2012 gave distributors the option to use the WCA rate of 13% or to complete a lead/lag study. Since KWHI did not do a lead/lag study, nor was it directed to do so, it utilized the 13% rate, in compliance with the OEB Filing Requirements.

17. Section 2.5.1.4 of the OEB Filing Requirements issued June 28, 2012 (Allowance for Working Capital) stated:

> *"the applicant may take one of two approaches for the calculation of its allowance for working capital (1) the 13% allowance approach; or (2) the filing of a lead/lag study. The only exception to the above requirement is if the applicant has been previously directed by the Board to undertake a lead/lag study on which its current working capital allowance is based."* (Page 17)

[4] EB-2009-0267, page 27

18. Since KWHI was not directed to do a lead/lag study, KWHI had the choice of option (1) or option (2), and chose option (1).

19. The options set out above are unchanged in the most current version of the OEB Filing Requirements, issued July 17, 2013.

20. KWHI's Application, as originally filed, anticipated a move to monthly billing for its Residential and GS<50kW customers in the latter half of the 2013 Bridge Year. Had KWHI conducted a lead/lag study, KWHI submits that the results may not have been indicative of what would occur under monthly billing since the study would have been based on KWHI's current practice of bi-monthly billing.

21. It is KWHI's understanding that the Board, on its own accord, conducted a Board-led process to determine the revised WCA of 13%. To KWHI's knowledge, the Board did not solicit input from electricity distributors prior to issuing its April 12, 2012 letter. However, KWHI respectfully submits that the Board clearly turned its mind to the question of an appropriate default WCA percentage factor and, in its letter of April 12, 2012 and the subsequent amendment to the OEB Filing Requirements, reduced that value from 15% to 13%. KWHI reasonably understood that letter to mean that it was not required to complete a lead/lag study for its next Cost of Service Application. Since the OEB Filing Requirements were updated to include the WCA of 13%, as per the Board's letter, KWHI submits that its use of the 13% WCA is appropriate.

ISSUE 2.2: IS THE WCA FOR THE TEST YEAR APPROPRIATE?

22. In its Application, and as noted above, KWHI requested a WCA of 13% of the eligible controllable expenses including property taxes and cost of power. This request is consistent with the OEB Filing Requirements. The OEB Filing Requirements suggest one of two approaches for the calculation of the allowance for working capital – the 13% allowance approach or filing a lead/lag study. KWHI did not conduct a lead/lag study, as it

was not directed to do so by the Board and relied on the OEB Filing Requirements to set a rate.

Board Staff and Intervenor Submissions:

23. Board staff submits that KWHI's reliance on the updated default WCA factor of 13% is reasonable.

24. Energy Probe submits the percentage is too high because of the move to monthly billing for KWHI's Residential and GS<50kW customers.

25. VECC submits that the WCA should be no higher than London Hydro's 11.4%.

26. SEC suggests the WCA should be reduced to 9% as a result of the move to monthly billing for KWHI's Residential and GS<50kW customers or, in the alternative, that if monthly billing for KWHI's Residential and GS<50kW customers were excluded from the OM&A expenses, the WCA could remain at 13%.

KWHI's Reply:

27. KWHI offers the following reply submissions in this regard:

   a. KWHI filed its Application in accordance with the OEB Filing Requirements as issued on June 28, 2012 and July 17, 2013.

   b. KWHI used the results of a Board letter dated April 12, 2012 as allowed by its Decision (EB-2009-0267) in 2010.

   c. The Board has not performed another study since the letter was issued; therefore, KWHI relied on the direction of this letter, and the OEB Filing Requirements.

d. KWHI has not yet converted its Residential and GS<50kW customers to monthly billing.

e. Recent Decisions by the Board (Sioux Lookout EB-2012-0165, Centre Wellington EB-2012-0113, Co-operative Hydro Embrun EB-2013-0122 and Hydro Hawkesbury EB-2013-0139) support the use of the 13% WCA even with monthly billing.

28. KWHI did not perform a cost benefit analysis for moving its Residential and GS<50kW customers to monthly billing. KWHI's anticipated move to monthly billing for these customers was due to the following factors:

a) KWHI understood that monthly billing may be mandated by the Minister of Energy[5] in the near future; and

b) Convenience and easier budgeting for its customers due to smaller electricity bills[6], leading to higher customer satisfaction.

29. Energy Probe is focusing on one part of the equation (Service Lag) for the calculation of its suggested WCA for KWHI, which ignores Expense Leads that may be unique to KWHI. KWHI notes that the Expense Leads are different for London Hydro and Horizon Utilities. London Hydro had a PILS Lag[7] and Horizon had a PILS Lead[8]. Horizon had an Interest Lag[9] while London Hydro[10] had an Interest Lead. Without having performed a precise analysis or a thorough lead/lag study, one cannot assume what KWHI's Expense Leads will be.

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[5] TR. Vol. 1,page 49, line 8, page 52, line 26, page 53, line 3, page 114, line 22, page 118, line 6
[6] Exhibit 4, Tab 2, Schedule 2, Page 4
[7] EB-2012-0146 Exhibit 2, Appendix 2-J, page 16
[8] EB-2010-0131 Exhibit 2, Tab 4 Schedule 1, page 14
[9] EB-2010-0131 Exhibit 2, Tab 4 Schedule 1, page 14
[10] EB-2012-0146 Exhibit 2, Appendix 2-J, page 16

30. SEC argues that the Service Lag will be reduced and that the remaining elements of the working capital calculation are irrelevant. KWHI submits that each LDC that has filed a lead/lag study has had unique Expense Leads and Lags as can be shown below in Table 1:[11]

Table 1 Expense Leads

LDC	File Number	Cost of Power	OM&A Expenses	PILS	Interest Expenses	Debt Retirement Charge
London Hydro	EB-2012-0146	32.12	15.08	(28.76)	47.29	31.33
Hydro One	EB-2009-0096	32.67	22.92	16.51	52.87	52.87
Toronto Hydro	EB-2007-0680	32.61	19.86	37.95	43.23	33.20
Hydro Ottawa	EB-2011-0054	33.67	11.18	(3.31)	45.63	32.69
Horizon	EB-2010-0131	32.77	13.74	34.44	(62.74)	28.27

These Expense Leads are subtracted from the Service Lag to result in net lag days. These net lag days are weighted to the related expense item to determine a WCA.

31. There is a difference of 66 days between the PILS Expense Leads of the above distributors and 115 days in Interest Expense Leads. KWHI therefore submits that the remaining elements are relevant and that each LDC is different.

32. KWHI has not yet converted its Residential and GS<50kW customers to monthly billing. While it had planned to do so, its ability to convert to monthly billing will depend in part on whether the Board's determination of its OM&A request allows it enough funds to cover the expenses associated with the transition. If KWHI does not move its Residential and GS<50kW customers to monthly billing, then any discussion or calculation of Service Lags is no longer valid and the WCA should remain at 13%.

[11] Energy Probe Compendium, pages 48(Horizon),page 50 (Hydro Ottawa), page 53 (Toronto Hydro),page 56 (Hydro One), page 59 (London Hydro)

33. Another view of WCA is the actual WCA as calculated based on information in the OEB Yearbooks. Based on information found in the OEB Yearbooks, KWHI's actual WCA for the years 2010 through 2012[12] would have been as shown below in Table 2:

Table 2 Working Capital Allowance

	2012	2011	2010
Current Assets (1)	61,937,740	64,268,511	67,838,721
Current Liabilities (2)	30,204,233	29,548,384	28,369,319
Cost of Power (3)	170,281,848	163,084,890	156,940,481
Operations (4)	4,821,308	3,258,635	2,824,720
Maintenance (5)	5,226,753	4,856,219	4,069,611
Administration (6)	6,779,135	5,492,367	5,376,627
Actual Working Capital Allowance as at December 31st	17.0%	19.7%	23.3%

WCA is calculated as [(1) – (2)] / [(3) + (4) + (5) + (6)]

34. The WCA results calculated above in Table 2 are higher than the previously deemed 15% WCA that was built into KWHI's rates in its last Cost of Service[13] and higher than the 13% WCA deemed by the Board letter of April 12, 2012. KWHI notes that these figures do not include the effects of monthly billing.

35. In the Board letter of April 12, 2012, the Board stated:

"the Board has determined that it is not appropriate for a default value for WCA to be set at a higher level that those resulting from lead/lag studies"

36. KWHI is not requesting a higher WCA than is deemed by the Board. The deemed Board rate does not distinguish between monthly and bi-monthly billing. Since KWHI did not do a lead/lag study, it is requesting the Board's deemed rate, which was set following a Board-led study.

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[12] OEB Yearbook, 2010, page 19 and 33
OEB Yearbook, 2011, Page 19 and 33
OEB Yearbook, 2012, page 19 and 33

[13] EB-2009-0267, page 26

37. In recent Board Decisions[14] for Centre Wellington (EB-2012-0013), Co-operative Hydro Embrun (EB-2013-0122), and Hydro Hawkesbury (EB-2013-0139), the Board accepted the use of 13% for WCA as it is consistent with Board policy and there is no compelling reason to depart from that policy. The Board states in its Decisions that it is reluctant to adopt the results of a lead/lag study from one utility to another without a thorough analysis of the circumstances for each utility. All of these LDC's bill monthly.

38. KWHI respectfully submits that the information set out above clearly illustrates the importance of not simply applying the results of one utility's lead/lag study to another. In the absence of a lead/lag study for KWHI, KWHI submits that the Board's default percentage factor of 13% should be used in calculating KWHI's WCA.

39. KWHI notes that Board staff suggest[15] that a consultation or working group could be considered to conduct a more extensive and generic study on an appropriate working capital allowance for distributors moving to monthly billing. They state "*it may be appropriate to do this in about a year or so, when more distributors, including KWHI, may have converted to monthly billing and may have better information on the leads and lags of costs and revenues with this change.*" KWHI submits that this would be a more appropriate approach than the arbitrary adjustments suggested by the intervenors.

ISSUE 4.1: IS THE OVERALL OM&A FORECAST FOR THE TEST YEAR APPROPRIATE?

40. The evidence for KWHI's OM&A claim is presented in Exhibit 4, various Interrogatories, Technical Conference questions, and Undertakings. The Evidence in Chief and Argument-in-Chief also support KWHI's claim.

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[14] EB-2013-0122 Co-operative Hydro Embrun, Decision and Procedural Order December 23, 2013, page 4
EB-2012-0113 Centre Wellington, Decision and Order May 23, 2013, page 4
EB-2013-0139 Hydro Hawkesbury, Decision and Order January 30, 2014, page 10

[15] Board Staff Submission, January 23, 2014, Page 4-5

41. KWHI has requested an overall increase in rates of 0.3%[16] or $130,436 in additional revenue. Included in this request is the OM&A request of $18,480,760.

42. The details of the various adjustments proposed by KWHI in respect of its OM&A request are noted in the Table 3 below:

Table 3

Reference	Item	OM&A
Original Application, Exhibit 4		18,523,200
4-Energy Probe-66	Update Inflation	(11,200)
JT1.6	Additional Inflation	(31,240)
		18,480,760

43. New initiatives that are planned or have been undertaken by KWHI in the past 4 years include monthly billing ($401,500),[17] ash tree removal ($100,000),[14] a new Human Resource Specialist ($123,099),[18] a Communications person ($98,000),[19] and Smart Meters ($352,000)[20].

Board Staff and Intervenor Submissions

44. Board staff asserts that proper maintenance of vegetation is the responsibility of the property owner (including municipal, provincial or federal governments in the case of trees on public property). Board staff further states that the ongoing trimming of trees is a necessary distribution activity. Board staff concludes that the expense of $100,000 for removing ash trees should be denied by the Board as the overall responsibility for removal of the ash tree is the responsibility of the owner.

[16] TR. Vol. 1, page 24, line 10
[17] Undertaking Responses, Undertaking JT1.15
[18] Exhibit 4, Appendix 2-J
[19] TR. Vol. 1 page 140, line 25
[20] Exhibit 4, Appendix 2-J

45. Board staff submits that $300,000 of the $401,500 incremental monthly billing should be removed to reflect the offsetting cost efficiencies and improved cash flow from monthly billing.

46. Energy Probe and VECC submit that an envelope approach to OM&A is appropriate. Energy Probe submits a reduction to OM&A of $1,656,138 based on an average of three methods.

47. VECC submits that an envelope approach to OM&A is appropriate. VECC proposes a reduction of OM&A in a range between $1,095,679 if KWHI's Board-Approved actuals are used, to $2,722,652 if KWHI's Actuals for 2010 is the starting point.

48. SEC also submits an envelope approach is suitable, but recognizes that KWHI is a low cost distributor. Therefore, SEC suggests removing $880,760 from the OM&A budget to reduce it to $17,600,000 and reducing the WCA to 9%. SEC also proposes returning to 2008 and to define 2008 as a typical year for KWHI.

49. An alternative position from SEC is to reduce the OM&A budget to $17,200,000 by backing out the incremental cost of monthly billing, and allow the 13% WCA to stand.

50. VECC argues that membership in the Electricity Distributors Association is largely a benefit to the municipal owners, and some costs such as MEARIE Insurance should be subject to greater scrutiny.

KWHI's Reply:

- **ASH TREE REMOVAL**

51. Board staff has argued that "proper maintenance of vegetation is the responsibility of the property owner (including municipal, provincial or federal governments in the case of trees on public property)." KWHI, however, has no authority to direct property owners to

remove dead ash trees. KWHI submits that under Ontario law, it is also the responsibility of the distributor to maintain the trees where the trees are found in proximity to a pole line.

52. Ontario Regulation 22/04 made under the *Electricity Act, 1998* sets out the safety standards that must be met by LDCs operating electricity distribution systems in Ontario. In general terms, subsection 4(2) of the Regulation provides that "All distribution systems and the electrical installations and electrical equipment forming part of such systems shall be designed, constructed, installed, protected, used, maintained, repaired, extended, connected and disconnected so as to reduce the probability of exposure to electrical safety hazards."

53. More particularly, Paragraph 4(3)3 establishes the following requirements for vegetation management: *"**Energized conductors** and live parts **shall be barriered such that vegetation**, equipment **or unauthorized persons do not come in contact with them** or draw arcs **under reasonably foreseeable circumstances**."* (Emphasis added). Within the context of the Regulation, separation sufficient to prevent contact under reasonably foreseeable circumstances is considered to be an adequate barrier. Note that the Regulation requires action by the LDC regardless of who owns the land that the trees are on.

54. KWHI agrees with Board staff that ongoing tree trimming is a necessary distribution activity and KWHI submits that the removal of dead ash trees and the hazards that they pose to the safe and reliable operation of KWHI's overhead lines is a reasonable and appropriate part of this program. The Emerald Ash Borer problem has been identified as a problem in the City of Kitchener and surrounding area. The City of Kitchener plans to spend up to $6.7 million in the next 10 years to remove ash trees[21]. The $100,000 program identified by KWHI is to remove trees near pole lines that will affect the reliability and safety of its distribution system.

55. Ash tree removal is different than other tree trimming activities that are undertaken by KWHI arborists. KWHI's current tree trimming program trims branches near wires. Ash

[21] http://www.kitchener.ca/en/livinginkitchener/EAB.asp

trees pose a significant threat to poles and wires, because the roots of an ash tree give out when the tree dies, allowing the tree to fall on anything in its path. It is dangerous to cut down an already dead ash tree. Ash trees die quickly once infected. If KWHI is not proactive in mitigating this threat, KWHI will see increased pole line repair costs, increased outages and increased risk to the public. Accordingly, KWHI respectfully requests that the amount budgeted for ash tree removal not be removed from Board-approved OM&A.

- **MONTHLY BILLING**

56. KWHI submits that the $300,000 reduction that Board staff suggest removing from OM&A representing in part the benefits of monthly billing and in part because monthly billing has not commenced, is an arbitrary figure. KWHI does not know what the benefits from monthly billing are[22], if any, and any amount of benefits attributed to monthly billing is at best, speculative. As KWHI stated at the Oral Hearing, until such time as monthly billing is implemented, any benefits streaming from the implementation of monthly billing are difficult to quantify[23]. There is no evidentiary support for this $300,000 figure for the benefits of monthly billing. KWHI respectfully requests that Board allow recovery of the full forecasted cost of $401,500 for monthly billing without offsets for anticipated benefits.

57. KWHI also notes that despite the fact that monthly billing of KWHI's Residential and GS<50kW customers has not yet commenced, additional annual costs to move to monthly billing will be $499,500 per year after factoring in the most recent Canada Post announcement of significant increases in postage charges. KWHI asked for $401,500[24] for the incremental costs of monthly billing. As discussed in the Oral Hearing, these costs have changed by an estimated $98,000[25] with the recent Canada Post announcement, but these additional costs have not been incorporated into KWHI's OM&A request. KWHI is

[22] Interrogatory, October 15, 2013, 2-VECC-2, 4-Staff-20b) and 4-Energy Probe-38
[23] TR. Vol. 1 page 117, lines 7-9
[24] Undertaking, November 6, 2013, JT1.15
[25] TR. Vol. 1 page 39, line 8

prepared to absorb the additional $98,000 in postage costs related to monthly billing, but arbitrary reductions to the amount requested in respect of monthly billing will make is far more difficult for KWHI to do so. The Board staff approach would, in effect, allow KWHI only an amount equivalent to the incremental postage rate increase recently announced by Canada Post, and it will make it far more difficult to provide monthly billing to KWHI's customers in the 2014 Test Year and beyond. KWHI respectfully submits that there is no basis for this reduction in the evidence before the Board.

58. While KWHI agrees that the move to monthly billing is a benefit to the customer, arbitrary offsets that would effectively eliminate the expense on monthly billing from KWHI's revenue requirement may cause KWHI to abandon the initiative.

- **OM&A GENERAL**

59. Through the last rebasing cycle, KWHI has operated under the IRM approach. However, in the last four years; however, KWHI has or will introduce the following new programs[26] as shown in Table 4 below:

Table 4

HR Specialist	123,099
Monthly Billing	401,500
Ash trees removal	100,000
Animal Proofing	150,000
Communications Person	98,000
Disaster Recovery	66,000
Smart Meter	352,000
	1,290,599

60. KWHI added a new transformer station in 2010 with it becoming fully operational in 2011. As can be seen by Appendix 2-G, the operating costs on one transformer station can be estimated as:

[26] Exhibit 4, Appendix 2-J, Evidence in Chief

Table 5

OEB Account	Description	2010	2014	Cost of one station 2010	Cost of one station 2014
5014	Transformer Station Equipment - Operation Labour	281,354	294,700	40,000	37,000
5015	Transformer Station Equipment - Operation Supplies and Expenses	553,544	647,500	79,000	81,000
		834,898	942,200	119,000	118,000

61. During the first year of operations, the new transformer station would incur minimal costs for maintenance. To calculate the estimated maintenance costs of one transformer station, using the information in Appendix 2-G, the estimated cost of maintaining one transformer station is calculated as:

Table 6

OEB Account	Description	2011	2014	Cost of one station 2011	Cost of one station 2014
5110	Maintenance of Buildings and Fixtures - Distribution Stations	149,303	183,000	21,000	23,000
5112	Maintenance of Transformer Station Equipment	579,330	748,100	83,000	94,000
				104,000	117,000

62. In the last rebasing cycle, KWHI has completed the construction of one transformer station and has incurred additional costs related to the operation and maintenance of this station. Although KWHI does not measure the costs of operating and maintaining one transformer station separately, KWHI estimates the annual cost of maintaining an additional transformer station to be approximately $220,000 per year. The operating and maintenance costs for the new transformer station are fully incremental to KWHI's 2010 Board-approved revenue requirement. As discussed below in paragraph 76, KWHI's construction and ownership of the transformer stations adds to the OM&A costs, but results in significant savings to KWHI's customers on retail transmission service rates.

63. KWHI understands that in previous of Cost of Service applications, the Board has applied a formula for OM&A that uses factors for inflation, customer growth and productivity/stretch factor. As Mr. Van Ooteghem noted in his Evidence-in-Chief[27], during the last rebasing cycle, KWHI has faced unprecedented increases to its operating costs that far exceed the formula of inflation plus growth. KWHI lists a few of those

[27] TR. Vol. 1, page 29, lines 17-21

incremental costs below, but note that Table 7[28] is not exhaustive. Many other costs have increased at a rate that exceeds the rate of inflation, but the individual costs are not material. Taken together they become significant costs to the utility.

Table 7

	2014 Test	2010 Actual	Increase	% Increase
Insurance	524,100	328,614	195,486	59%
OMERS	986,207	558,195	428,012	77%
Rebasing Costs (Amortized over 4 years)	68,125	40,515	27,611	68%
	1,578,432	927,323	651,109	70%

64. The costs shown above in Table 7 are third party costs over which KWHI has no control. If these third party costs increased by 2.67%[29] per year, the 2014 cost would be $1,030,399. The 2014 forecasted costs are, however, $1,578,432, representing an excess cost of $548,033 as shown in Table 8 below. These excess costs continue to increase at rates higher than inflation, and during the IRM period, KWHI must find internal efficiencies in order to continue to operate profitably while also providing a reliable and safe power supply to its customers.

Table 8

	2010 Actual	Assumed 2014 Test at 2.67% / year	2014 Test	Excess costs
Insurance	328,614	365,141	524,100	158,959
OMERS	558,195	620,240	986,207	365,967
Regulatory Costs	40,515	45,018	68,125	23,107
	927,323	1,030,399	1,578,432	548,033

65. Based on the discussions above, KWHI is facing three distinct cost pressures:

[28] Insurance costs from Appendix 2-G, OEB accounts 5635 & 5640
OMERS costs from Exhibit 4, Tab 4, Schedule 1, Page 11 – less 35% burdened to capital
Regulatory costs from Exhibit 4, Appendix 2-M
[29] Energy Probe Argument, Page 14, Table 4

a. Increases beyond the rate of inflation (i.e. OMERS, Insurance, Regulatory)
b. Increases for new programs (i.e. monthly billing, smart meters, HR specialist)
c. Increases due to additional operating pressures (i.e. new transformer station)

66. 2010 was an unusually low year for OM&A costs due to labour resources being diverted from OM&A to capital projects[30]. As stated by KWHI in its Evidence-in-Chief, it is difficult for KWHI to determine a "typical year"[31] in terms of OM&A. KWHI's 2010 Board approved OM&A was different from its actual results due to the diversion of resources to capital projects, retirements, and the collection of bad debts. When KWHI budgets for a Test Year, the expectation is that the Test Year will be typical. Accordingly, KWHI suggests that it would be appropriate to consider the 2010 Board Approved values as representing a typical year.

67. If KWHI assumes that Board Approved amounts from 2010 represent a typical year, and uses the escalator factor as calculated by Energy Probe in its Argument[32] of 2.67% and then factors in additional costs pressures in excess of inflation, additional operating costs and the addition of new programs, the total is as presented in Table 9 below:

Table 9

2010 Board Approved	13,881,502	From EB-2009-0267
Inflation/Growth/Productivity	1,542,984	From Energy Probe Argument Pg 14 Table 4
Transition costs - OLD GAAP to NEW GAAP	1,692,337	from 4-Energy Probe 68
Cost Pressures in excess of inflation:	548,033	Table 7
New Operating Costs	220,000	Additional Transformer Station
New Programs	1,290,599	Table 5
	19,175,455	

68. KWHI has requested $18,480,760 for the 2014 Test Year, almost $700,000 less than would be suggested by the Table 9 above. Put another way, KWHI is able to add several new programs ($1,290,599); address cost pressures in excess of inflation ($548,033); and operate an additional transformer station ($220,000) with an OM&A request in the

[30] TR. Vol. 1, page 25, line 2
[31] TR. Vol. 1, page 24, line 26
[32] Energy Probe Argument, Table 4, page 14

Application that is lower than that which would result from the use of a formulaic approach. KWHI respectfully submits that this is because it is an efficient operator. The OM&A request contained in this Application provides the funds needed for the continued safe and reliable operation of the KWHI's distribution system and the addition of appropriate new programs with minimal bill impacts.

69. KWHI respectfully submits that using actual dollars from a specific year as a starting point for applying the envelope approach does not recognize the variations in each year. SEC used the year 2008. VECC used 2010. KWHI would argue that a "typical year" is hard to find in a LDC, due to such factors as weather, capital projects and mandated programs, and for the reasons discussed during the Oral Hearing, it is particularly difficult for KWHI to determine a "typical year." Maintenance schedules are cyclical in nature, and can have variations year over year. When forecasting for a Test Year, KWHI plans for a "typical" one.

70. The formulaic envelope approach also does not recognize when an LDC needs to play catch up. As an example, most LDCs of KWHI's size have had Human Resource departments for years. KWHI recently added this important resource to its staff complement. KWHI has also only recently implemented a Disaster Recovery Program, an additional expense of $66,000, the cost of which was found through KWHI's internally generated efficiencies.

71. The envelope approach assumes that each LDC is operating in an environment where it is assumed that all LDCs are operating with the same in terms of programs, operations and efficiencies. This is not true as KWHI owns and operates all of its transformer stations. Further, KWHI did not have a Human Resource department until 2012. KWHI is a low cost distributor as demonstrated by having the third lowest OM&A cost per customer[33]. The envelope approach assumes that all LDCs begin evenly in terms of efficiencies and

[33] 2012 OEB Yearbook, pages 69-81

have similar amounts that can be trimmed from their OM&A without affecting the safety and reliability of their operations.

72. The current formulaic approach considers only the costs incurred by the LDC and gives no weight to additional pressures faced by the utility or the efficiencies already gained. As an example, KWHI has faced increases in some of its OM&A costs in excess of 70%. Further, it has incurred the costs of operating an additional transformer station and smart meters. These costs alone are greater than the stretch factor applied to KWHI's distribution revenue requirement. By applying a stretch factor on a general envelope, there is no recognition of the cost savings already achieved, nor room for additional programs. The envelope approach further does not allow utilities to expand current programs while continuing to maintain the reliability and safety of the current distribution system.

73. For the above reasons, applying a formula to a base year actual and expecting a utility to operate and maintain its system within that envelope, does not give recognition to the individual cost pressures faced by a utility, particularly a low cost, high performing one. The envelope approach does not give the LDC the flexibility to undertake additional programs that would increase benefits to its customers (i.e. monthly billing or additional vegetation management) or mandated programs (i.e. Smart Meters and Ontario One Call).

74. In order to calculate the OM&A cost per customer, KWHI relies on the information contained in the OEB Yearbook. The source of the information in the OEB Yearbook is distributors' RRR filings.

75. KWHI has the third lowest OM&A per customer in 2012 at $189.02[34]. Using the 2014 proposed OM&A of $18,480,760 and the year-end customer count projected for 2014 of 91,353[35], KWHI's OM&A per customer will be $202.29. Comparing this $202.29 per customer for 2014 to the 2012 OEB OM&A per customer yearbook numbers for all LDCs,

[34] 2012 OEB Yearbook, page 77
[35] Exhibit 3 Tab 1, Schedule 4, Page 13, Table 3-22

KWHI would still be the 5th lowest LDC in the province. KWHI's increase in OM&A per customer would be 7% from 2012, or an average of 3.5% per year. It should be noted that KWHI's customer growth for this same period is 1.5%[36]

76. KWHI's OM&A per customer in 2012 includes $18.87 per customer for operating eight transformer stations. As mentioned during the Oral Hearing[37], KWHI is one of the few LDCs that owns and operates transformer stations for its customers. For KWHI the full cost of the high voltage transformation is included in the distribution OM&A amount which is reflected in KWHI's distribution rates. For other LDC's this cost is included in their retail transmission service rates for connection. As a result, in a case where an LDC is similar in size to KWHI their OM&A would not include the cost of service for high voltage transformers but their retail transmission rates for connection would include around $6.8 million more in costs as this represents the annual savings resulting from KWHI owning the high voltage transformers. KWHI notes that it has maintained its low OM&A costs even though the cost of operating its eight transformer stations – a cost that other LDCs do not have – is embedded in its OM&A. These represent significant costs for which KWHI has, in essence, been penalized when being compared to other LDCs in the Province of Ontario – notwithstanding this, though, KWHI has maintained its position as a low cost performer due to its continual drive for finding internal efficiencies. The approval of KWHI's OM&A as requested will not change this status nor KWHI's continual drive to achieve efficiencies.

77. KWHI OM&A per customer in 2012 also reflects the Smart Meter Decision (EB-2012-0288) and the change in accounting estimates. Per customer these amounts were $12.18 and $19.01 respectively. Removing these amounts from the published $189.02 per customer results in an amount of $157.84 per customer. KWHI's OM&A per customer in 2011 was $154.69[38]. The increase is $3.15 or 2.0% for the year.

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[36] Settlement Proposal, Table 3-1, page 64
[37] TR. Vol. 1, page 22, lines 8-20
[38] 2011 OEB Yearbook, page 75

78. KWHI is proud of its standing among its peers. KWHI has had this high standing since the OEB began comparing LDC's for the purpose of stretch factor assignment. KWHI submits that it has significant cost pressures that it has, for the most part, successfully been able to bear but that the formulaic envelope approach is not appropriate for this LDC. KWHI has had a high ranking when compared to its peers year over year and this demonstrates that KWHI has only limited capabilities when it comes to driving further efficiencies. Since it is already working efficiently, there are fewer places where costs can be reduced without affecting the safety and reliability of KWHI's system. KWHI will continue to drive efficiencies where it can find them; however, when uncontrollable base costs are increasing faster than the rate of inflation plus growth less a productivity factor, KWHI has only limited capacity to keep its OM&A as low as the above factor would calculate.

- **EDA AND MEARIE**

79. KWHI submits that membership in the EDA provides benefits for LDCs that are not just for the benefit of the shareholder. Members are provided with up to date analyses of legislation and market rules, networking opportunities, and advocacy and representation in the legislative and regulatory environment. This allows distributors to have superior knowledge and to respond timely to regulatory matters, including better Cost of Service Applications, lightening the load for both Intervenors and the Board. As Mr. Van Ooteghem said[39]

"If we had to do that ourselves individually, we could not afford to do that. We don't have the staff to do it, to participate, and this is a cost-effective way for us to participate and give our views and inputs on some of these proceedings."

80. With respect to MEARIE, the MEARIE Group is the only Canadian insurance supplier dedicated to the electricity distribution sector. It offers comprehensive product coverage not readily available in the commercial market. Rates are reflective of member experience and not pooled with other industries.

[39] TR Vol. 1, page 108, lines 20-24

81. The driver of the cost increase in the insurance premiums is the adjustment to the Total Insured Value (TIV). As the TIV increases, so too do the premiums. KWHI's TIV increased by $72 million since 2009 or 89%. The premiums have increased by 67%.[40] Note that KWHI was underinsured in 2010, which could have resulted in significant bill impacts to its customers in the case of a severe event.

82. KWHI respectfully submits that there is no basis for the additional scrutiny advocated by VECC in this proceeding. The expenses related to the EDA and MEARIE are substantiated in the evidence, the insurance expenditures allow for the adequate protection of the utility's assets, and EDA membership assists in the efficient operation of the utility (including its economically efficient operation). These expenses are routinely allowed by the Board as part of OM&A and KWHI respectfully submits that if the Board were to determine that further consideration is warranted (KWHI submits that it is not), this proceeding is not the appropriate forum. Matters such as those being raised by VECC may affect the entire distribution sector and it would be entirely inappropriate to consider VECC's assertions in the context of a single Cost of Service proceeding.

- **FORECASTS**

83. Energy Probe submitted that KWHI's costs increased from November 2012 to November 2013 by 1.6% and suggests that 2013 expenses will therefore be 1.6% higher than 2012. KWHI disagrees with this as there are many year-end adjustments. These include, but are not limited to, true-ups of payroll burdens, accruals of year-end expenses, and account reconciliations.

84. KWHI uses a bottom up approach to budgeting; however, the entire budget (both Capital and OM&A) must pass the scrutiny of the CEO[41] and KWHI's Board of Directors. Senior managers are given guidance as to how much of a percentage increase to expect. In 2014,

[40] Undertaking JT1.18, November 6, 2013, page 27
[41] TR. Vol. 1, page 150, lines16-17

this percentage was set at 2%[42]. Each manager budgets for the controllable costs relevant to their department. Some maintenance programs are cyclical in nature, so costs vary year over year. Costs that are beyond the control of the managers, such as payroll burdens are planned for by the Accounting department.

85. Energy Probe submits that in KWHI's Decision and Order (EB-2009-0267) dated April 7, 2010 the Board stated:

> *"The Board finds it useful to look at OM&A levels from a number of perspectives: the specifics of the test year forecast; trends in spending over time, expectations for inflation and economic conditions; and comparisons with other distributors."*

86. Energy Probe concurred with the comments, and then qualified this by saying it was not possible to compare the specific spending forecast for the Test Year to the years prior to 2012 due to accounting changes and the Smart Meter Decision (EB-2012-0288).

87. KWHI submits that this is possible and points to its completed version of the Board's Appendix 2-G, filed in its original Application. That Appendix contains a line by line comparison year over year. As stated by Ms. Nanninga[43], Appendix 2-G is very helpful at the account level detail. Appendix 2-G details specifically where increases have occurred.

88. Since a line by line comparison can be done at an account level, one can see where cost pressures have been faced by KWHI and where the forecasted increases are expected to occur. KWHI has explained these forecasted increases in the evidence in this proceeding.

89. It can be seen that even with accounting changes and the Smart Meter Decision (EB-2012-0288), some business units have minimal increases or decreases to expenses (i.e. OEB Accounts 5016 and 5075), some accounts have larger increases explained by new programs (i.e. OEB Accounts 5315 and 5320 – monthly billing) and some have very large increases (i.e. OEB Accounts 5635 and 5640 – Insurance increases).

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[42] TR. Vol. 1, page 20, line 4
[43] TR. Vol. 1, page 2,1 lines 10-11

90. KWHI has been very successful at maintaining its costs within its budget for the year which is adjusted in Q4. KWHI incurs a disproportionate amount of OM&A expenses in the final quarter of the year and notes that the actual year to date numbers incurred by KWHI may not be an indicator of what the final year end actual numbers will be.

CONCLUSION

91. KWHI submits that the WCA requested is reasonable, follows Board Policy, and therefore should be approved at 13% as submitted.

92. KWHI submits that its requested OM&A, in the amount of $18,480,760, is just and reasonable, and requests that the Board approve this value and direct KWHI to prepare a draft Rate Order that implements the requested OM&A into the rate model.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 6th DAY OF FEBRUARY, 2014.

Jerry Van Ooteghem. P. Eng

President and CEO
Kitchener-Wilmot Hydro Inc.