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BY EMAIL and RESS

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Ontario Energy Board
2300 Yonge Street
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Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2018-0328 – Halton Hills Hydro Inc. – SEC Submissions

We are counsel to the School Energy Coalition ("SEC"). Pursuant to Procedural Order No. 1, these are SEC's submissions on the application by Halton Hills Hydro Inc. ("HHHI") for an incremental capital module ("ICM") related to the construction of a new transformer station ("TS").

As discussed in detail below, the evidence demonstrates that the proposed TS project meets the need, and materiality criterion, for an ICM.[1] With respect to the criteria of prudence, there is simply insufficient evidence to demonstrate that the project cost is prudent. In light of the need for the TS, and the recognition that at least most of the incremental funding is required, SEC submits the Board should approve an ICM rate rider on an interim basis or create a variance account. Doing so would allow for a full testing of the reasonableness of the specific project costs in a more fulsome manner at HHHI's next cost of service application.

The Proposed Project

HHHI is seeking an ICM for the revenue requirement impact of its proposed new TS that is expected to be in-service in the spring of 2019. The capital costs of the proposed TS is forecast to be approximately $23.5M, which after application of the Board's ICM model, would result in an incremental revenue requirement of $1.7M in 2019.[2] In addition, without citing any existing regulatory mechanism or precedent, HHHI is seeking recovery of what it claims are $131,515 in incremental OM&A costs related to the proposed new TS. In total, HHHI is seeking recovery of an additional $1.83M annually from ratepayers.[3]

SEC recognizes that a transformer station is the type of investment that is very lumpy. It requires an amount of capital to go in-service at once, while the load growth that it is meant to serve does not come on the system right away. This tends to lead to relatively large rate increases as compared to other type of projects. With that said, the distribution bill impacts of these projects are very significant, representing an average increase of 17.7% on the distribution bill.[4] When the formulaic

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[1] The test for an ICM is outlined in the *Report of the Board – New Policy Options for the Funding of Capital Investments: The Advanced Capital Module*, EB-2014-0219, September 18, 2014, p.17
[2] Pre-filed Evidence, p.20
[3] Pre-filed Evidence, p.21
[4] Interrogatory Response SEC- 9

price cap IRM adjustment is included, HHHI's customers are being asked to pay an additional 18.9% in distribution rates in 2019.[5] Due to both the $23M capital cost and the very significant distribution bill impacts, the project costs warrant very close scrutiny.

Need
The project meets the need requirement.[6] The new TS is a discrete project, outside the base upon which rates were set in its most recent cost of service proceeding (EB-2015-0074), required by the need for incremental capacity to serve the forecasted new load in HHHI's service territory.[7] HHHI has also met the means test as its return on equity is not above the 300 basis points threshold.[8]

SEC recognizes that constructing any new TS is a very costly capital investment and due to its inherently lump nature, will have a significant increase in rates in the near term. The evidence does demonstrate that the new TS is required to provide additional capacity to serve the growing load in Halton Hills.[9] A new TS to serve the incremental HHHI load was identified by the IESO as a preferred option in its Northwest Greater Toronto Area Integrated Regional Resource Plan ("IRPP").[10] The Halton Hills TS owned by Hydro One is nearing capacity and it cannot accommodate any additional feeders,[11] and the third-party load forecast confirms significant incremental capacity growth forecasted over the next decade in HHHI's service territory.[12] The evidence as of 2017 when the latest load forecast was undertaken for purposes of HHHI's decision to go ahead with the project is that at the latest, by the end of 2019, the new station would be required.[13]

Materiality
SEC agrees that the proposed project meets both the materiality tests that have surpassed the threshold value set by the Board's ICM formula.[14] In addition, it meets the project specific materiality test as the forecast costs are more than 3 times HHHI's annual capital expenditure forecast.[15]

Prudence
While SEC accepts that the new TS is required and the current location and configuration appears to be the preferred option, there is insufficient information on the record for the Board to approve the specific capital cost of $23.5M. SEC notes that in HHHI's 2016 cost of service application (filed in 2015) it had forecasted that the new TS would cost $19M, albeit with an earlier in-service date.[16] Soon after HHHI's Board of Directors were presented with a $21M forecast cost,[17] and by 2017 the forecasted amount approved by the Board of Directors amount had changed to $25.3M.[18]

While the requested $23.5M is less than the 2017 forecast, there is little evidence of the reasonableness of the amount.

Almost all of the application evidence on prudence relates to the need and reasonableness of a new TS option and that it can be constructed at the chosen location. There is almost no evidence to justify the reasonableness of a $23.5M cost. In approving an ICM, the Board is not just approving the

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[5] *Ibid*
[6] *Report of the Board – New Policy Options for the Funding of Capital Investments: The Advanced Capital Module*, September 18, 2014 (EB-2014-0219, p.17
[7] Pre-filed Evidence, p.10-12
[8] Interrogatory Response, Staff 1
[9] Pre-filed Evidence, Appendix D, p. 5.1
[10] Pre-Filed Evidence, p.1, Attachment C, p.56
[11] Pre-filed Evidence, Appendix D, p. 6.1
[12] Pre-filed Evidence, Appendix D, p. 5.1
[13] Pre-filed Evidence, Appendix D, p. 6.1
[14] Interrogatory Response, Appendix E
[15] Pre-filed Evidence, p.9
[16] Interrogatory Response, Appendix J, p.73
[17] Interrogatory Response Staff-4
[18] Interrogatory Response Staff-4; Interrogatory Response SEC-6; Interrogatory Response Appendix J, p.73

project, but that the cost consequences are just and reasonable. For example, HHHI did not provide any benchmarking analysis to show how the proposed costs for the new TS compare to similar projects undertaken in Ontario, or elsewhere. In response to Interrogatory Staff-4, HHHI relies on the fact that an “independent consultant” estimated the cost at the $25.3M, which is higher than its forecast cost.[19] It does not appear HHHI has provided this independent consultant’s estimate. The response simply refers to Interrogatory Staff-5, which points to the appendix which is simply a table of costs. The only consultant report that touches on project costs is the 2010 report from Costello Associates, which looks at various supply options and used a cost forecast of for a new TS to be $21M.[20]

There is insufficient evidence for SEC to come to the conclusion that the proposed costs of $23.5M are reasonable. While there is no evidence that the costs are unreasonable, it is the Applicant who has the statutory burden of proof to demonstrate prudence of the proposed costs to the Board.[21]

This leaves the Board and parties in a difficult position as there is a need for additional capacity and the project is expected to be completed shortly. The evidence is without ICM funding, due to the size of the project, there may be adverse impacts on HHHI’s financial viability as it will be offside on debt covenants with its lenders.[22]

SEC submits that in light of the establishment of project need, and that the specific option has been justified, the Board should allow HHHI to receive ICM funding, but defer a decision on the prudence of the costs until a more detailed review can be undertaken at its next cost of service proceeding. The Board can implement this approach by either approving the ICM on an interim basis, or alternatively, create a variance account to capture the difference of what is included in the ICM, and what may be approved after a full prudence review in a future proceeding. Proceeding this way would balance both the interest of ratepayers and HHHI.

Incremental OM&A Request
In addition to the capital costs of the new TS which HHHI is seeking to recover by way of the ICM, HHHI is seeking recovery of additional OM&A amounts related to the operations and maintenance (“O&M”) of the new TS. SEC submits the Board should deny this request.

First, HHHI has not identified any requital mechanism that would allow such recovery. The Board’s ICM policies make no mention of recovery of any amounts besides the incremental revenue requirements associated with capital costs (cost of capital, depreciation and PILs).[23] It is an incremental capital module, not an incremental capital, operations, and maintenance module. Whereas, the ICM has two materiality tests and a deadband calculation regarding how much ultimately can be recovered. HHHI does not even suggest a similar approach or calculation regarding what it claims are incremental O&M expenses.

Second, HHHI should expect to have offset O&M savings and incremental revenue to help recover any incremental costs it may have. There is usually some tradeoff between capital and O&M expenditures. SEC would expect that if the new TS is required to be in place in 2019, in part to

[19] Interrogatory Response Staff-4
[20] Interrogatory Response Appendix J, p.73 of 108
[21] *Ontario Energy Board Act, 1998,* s.78(8)
[22] Interrogatory Response Staff-3(b)
[23] *See* Report of the Board: New Policy Options for the Funding of Capital Investments: Supplemental Report (EB-2014-0219), January 22 2016; Report of the Board – New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014 (EB-2014-0219); Handbook to Utility Rate Applications, October 13, 2016, p.i

elevate overloading on the existing feeders[24], then one would expect a reduction in O&M expenses directly related to those existing feeders. This is one of the benefits of the proposed TS project.

Additionally, HHHI should recover additional base distribution revenue from the incremental load that the new TS will provide. This should offset any incremental O&M expenses that HHHI may have due to operating the new TS. The entire rationale of the new TS is that it is required to serve an incremental load. HHHI's own load forecast provided in the evidence, forecasts an increase in load from *new* loads (as opposed to load growth within the existing system) to equal over a 1 MW a year in each of 2019 and 2020.[25]

That incremental load will allow HHHI to collect incremental revenue. SEC asked what this additional revenue would be in SEC-IR 4. HHHI appeared to have misunderstood the question as in its response, while on one hand saying there would be zero incremental revenue it stated that due to forecast growth, it intends to use all additional capacity.

Lastly, the total increase in forecast O&M costs are not significant enough to require additional funding from ratepayers. They represent approximately 2% of its previously approved OM&A budget.[26] Considering that the ICM deadband is 10%, the amount requested would not meet a similar materiality threshold.

Yours very truly,
Shepherd Rubenstein P.C.

Original signed by

Mark Rubenstein

cc: Wayne McNally, SEC (by email)
Applicant and interested parties (by email)

[24] Pre-filed Evidence, Appendix D, p. 6.1
[25] Pre-filed Evidence, Appendix D, p. 5.1
[26] Interrogatory Response Staff-1