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BY EMAIL and RESS

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Ontario Energy Board
2300 Yonge Street
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Toronto, Ontario
M4P 1E4

Attn: Christine Long, Registrar

Dear Ms. Long:

Re: EB-2020-0133 – COVID-19 Deferral Account Consultation – SEC Reply Comments

We are counsel to the School Energy Coalition ("SEC"). These are SEC's reply comments on the OEB Staff Proposal ("Staff Proposal") as part of the *Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency*.

Overview

As SEC noted in our initial comments, the Staff Proposal is correct to recognize that the impact of the pandemic is of a fundamentally different character than other unexpected and extraordinary events that a utility may face. The situation does not have the hallmarks of a Z-Factor, because it is an economy wide downturn, and it impacts customers in many of the same ways as the utility. To the extent that the pandemic has caused impacts on a utility's costs and revenues, it has as much, or more so, impacted that utility's customers. Those customers, the ones from whom the utility would recover any deferral account balance, have been negatively impacted by their own increased costs and/or reduced revenues.[1] Many businesses are unable to pass on the increased costs and revenue losses through higher future prices, because their own customers are also financially hurting.

It is important to keep focused on the essential nature of any recovery from customers: it would give utilities greater protection from the pandemic than other businesses enjoy. This would be inconsistent with the Board's role as a proxy for competition.

The COVID-19 pandemic is requiring the Board to create a new approach to dealing with the impact on utilities, one that ensures both customers and utilities are treated fairly, and that is consistent with the objectives of electricity and natural gas under the *Ontario Energy Board Act.* A central component to the balancing of interests in the Staff Proposal was that "[r]ecovery of any balances recorded in the Account should be subject to evidence that the costs are not only reasonable, but also necessary to the maintenance of the utility's financial viability" [emphasis added][2]. OEB Staff referred to this as the

[1] OEB Staff Proposal, Consulting on the Deferral Account – Impacts Arising from the COVID-19 Emergency (EB-2020-0133), December 16, 2020, ["Staff Proposal"], p.10

[2] Staff Proposal, p.11

principle of necessity.

SEC's initial comments noted that, while OEB Staff laid out a principle of necessity, it did not adhere to that principle in its proposal. The Staff Proposal's Means Test parameters would have allowed financially healthy utilities to seek recovery of additional amounts from customers that were already suffering. This is, in our view, not appropriate. A 300 basis deadband below the deemed ROE included in a utility's base rates is not the point in which a utility's financial viability is at risk. This view is shared by most of the other ratepayer groups.[3]

Necessity and Financial Viability

The Ontario Energy Association/Coalition of Large Distributors+ ("OEA/CLD+") and the Electricity Distribution Association ("EDA") have taken the view that only the commonly used principles of causation, prudence and materiality for deferral and variance account creation/disposition should apply. Necessity in their view is new and untested, and so therefore should be rejected as a principle to be applied.[4] At the same time, the OEA/CLD+ and EDA do not propose that the Board utilize the existing Board mechanisms which apply those principles. They do not propose the Board limit recovery to those items that are eligible by way of a Z-Factor, but propose much more expansive categories of eligible costs. These utility stakeholders want to have it both ways.

As the Staff Proposal correctly points out, if the Board was looking at the COVID-19 pandemic through the lens of a Z-Factor event then, consistent with previous decisions, there would be no recovery for any amounts related to bad debt or lost revenue.[5] Based on the Board's most recent data on the balances recorded in Account 1509, approximately 60% of the combined balances in Account 1509 relate to these two items.[6]

These utility stakeholders want to use the principles that govern Z-Factor recovery, but without the related context and rules that also apply. SEC submits that, either the COVID-19 pandemic is a once in a generation event, which impacts both the utility and its customers, and so requires a different approach for the Board, or it is not, and the existing mechanisms for recovery (i.e. Z-Factor, off-ramps) are sufficient.

Predictably, the OEA/CLD+ and EDA want neither. These utility stakeholders instead recommend an unprincipled approach which would allow a greater scope of recovery than is either recommended in the Staff Proposal, or would be allowed under existing mechanisms for augmenting existing rates (Z-Factor, off-ramps, etc.). SEC fundamentally disagrees.

The proposed necessity principle recognizes the unique impact of the COVID-19 pandemic on both utilities and their customers. If implemented appropriately, it would ensure the financial viability of the sector and individual utilities, while at the same time protecting customers. If the utility is, or should be, able to manage the pandemic impacts, then it should do so. But, if a utility's ability to serve its customers is at risk, then additional recovery should be considered by the Board.

Fair Return Standard

Certain utility stakeholders take the view that the Staff Proposal, either directly or indirectly, breaches the Fair Return Standard, and thus is inconsistent with the Board's legal requirements in setting just and reasonable rates. SEC submits that this view simply misunderstands this consultation's place within the broader rate-setting context. Further, in any case, the evidence is that the Fair Return Standard is being met.

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[3] AMPCO/IGUA, para. 21-24, LPMA, p.9-10; CME, p.6; CCC, p.7; FRPO, p.4
[4] OEA/CLD+, p.12; EDA, p.9
[5] Staff Proposal, p.20-21
[6] See OEB, COVID-19 Account Balances Reported by Electric Utilities as of November 30, 2020

Legal Requirements. As AMPCO/IGUA correctly points out, the issue before the Board is not rate-setting in the usual context, but "whether relief from the rates already established is required on an immediate basis to address the exigencies posed to Ontario's regulated utilities by the COVID-19 pandemic."[7] Utilities' rates have already been set by way of an existing framework (i.e. cost of service + IRM or annual IR, Custom IR, etc.) and what is being determined now is what if any additional funding should be provided due to the pandemic (either because of additional costs and/or lower revenue).

It is under those existing rate-setting frameworks that the Board in setting those rates must ensure that the utility is given an *opportunity* to earn a fair return.[8] They have been given that opportunity. The issue that has arisen is that they may find it more challenging to earn that fair return, at least insofar as it is defined as their deemed ROE, due to an extraordinary change in the economy due to the pandemic.

But the Board is not required as a legal matter to ensure that a utility will at all times earn a fair return and recover its reasonably incurred costs. There will always be fluctuations up and down, some caused by matters that are entirely within management's control, and some that are not.

This was recently confirmed by the Divisional Court in *Halton Hills*[9], wherein the Court found that the Board made no error in not allowing, in the context of an ICM application, an adjustment for OM&A costs that the utility had to incur. It was sufficient that the Board undertook a full review of whether the overall rates were fair and reasonable every five years during a rebasing application.[10] This is consistent with the Supreme Court's comments in *OPG*[11], that what is required is that over the long run a utility must be given the opportunity to recover its reasonable costs but in "[i]n the short run, return on equity may vary".[12]

The Board in this consultation is seeking to create a set of guidelines under which it may allow an increase in customer rates to allow for additional recovery that is more than the utility would otherwise receive under their existing rate framework. The Board was not required to create Account 1509, and without the account there could legally be no disposition of any pandemic related costs/lost revenues. The fact that Account 1509 was created does not suddenly transform the issue to one about ensuring that the Fair Return Standard must be met. The OEB/CLD+ legal counsel report rightly points out that the Board was very clear when it created these accounts. There was no assurance that any or all of the lost revenues or incremental costs would be recoverable from anyone.[13]

Fair Return Standard Met. In addition, the evidence shows that the utilities are meeting the Fair Return Standard. LEI provided a full report that shows that on each of the various components and through various metrics, the publicly available information demonstrates that utilities continue to meet the Fair Return Standard, even with any additional costs and reduced revenues they are experiencing that are caused by the COVID-19 pandemic.[14]

The EDA questions the LEI analysis regarding the impacts of the pandemic on the cost of capital, and specifically the use of the S&P 500 index as a benchmark. SEC would simply note that if the LEI had used the TSX Composite Index or a similar Canadian-only index, the performance of utilities vis-a-vis

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[7] AMPCO/IGUA, para. 11
[8] *Ontario (Energy Board) v. Ontario Power Generation Inc*., 2015 SCC 44, para. 20
[9] *Halton Hills Hydro Inc. v. Ontario Energy Board*, 2020 ONSC 6085
[10] *Halton Hills Hydro Inc. v. Ontario Energy Board*, 2020 ONSC 6085, para. 24
[11] *Ontario (Energy Board) v. Ontario Power Generation Inc*., 2015 SCC 44,
[12] *Ontario (Energy Board) v. Ontario Power Generation Inc*., 2015 SCC 44, paras.16-17
[13]OEA/CLD+, Appendix A, p.13
[14] LEI, A Report on the OEB's Cost of Capital Parameters and the Impacts of COVID-19, p.10

that benchmark would have been significantly better than other companies, both before and during the pandemic.[15]

Additionally, the Board's deemed long-term debt rate continues to trend higher than what Ontario utilities of all sizes are actually getting in the market. Utilities are continuing to be able to secure long-term debt at rates that are materially below the current deemed long-term debt rate of 2.85%.[16] This is a good demonstration that the market continues to believe that Ontario utilities are a very safe investment, even with the impacts of COVID-19.

The Fair Return Standard is not the same thing as ensuring a utility earns the deemed level return on equity included in their rates. While at the time those rates are set, the Board's deemed ROE is meant to represent the Fair Return Standard, as market conditions change generally, that will impact the standard. Any consideration of Fair Return Standard in the context of the COVID-19 pandemic requires the Board to consider the impacts on utilities relative to the rest of the economy. The data is very clear – utilities may be worse off than before, but they have and continue to fare much better than almost all other businesses in the broader Ontario economy. The Staff Proposal showed that, through Q2 2020, the Ontario utility industry saw a reduction in GDP of 1.3%, whereas total production (i.e. output across all industries) declined by 12.4%, and many specific industries had declines that were much more precipitous.[17] The London Property Management Association ("LPMA") in its comments updated that information through Q3, and the results are that the cumulative Ontario GDP for the year was a decline in GDP of 3.4%, while utilities only saw a -0.4% GDP reduction.[18]

It is important to emphasize that stakeholders that seek higher levels of utility recovery are asking that the pandemic impacts the utilities have incurred be shifted off their backs, and onto the backs of customers that have already suffered significantly more than the utilities.

<u>Means Test For Financial Viability</u>

SEC does agree with the EDA that using achieved ROE as the only test for financial viability is unwise. As SEC noted in its initial comments, any attempt to make financial viability mechanistic is fundamentally incorrect. Financial viability is not by its nature formulaic. The EDA correctly notes that there are other aspects of a utility's financial situation that should be examined, such as their cash flow, current ratios, days cash on hand, return on assets, etc.[19] AMPCO/IGUA similarly noted in their comments that "there are commonly used liquidity and solvency measures (such as current ratios and interest coverage ratios) used by the Board which provide a better measure of continuing financial viability."[20]

SEC continues to recommend that the Board should not use a specific ROE deadband to determine financial viability. A more appropriate approach is that, if a utility believes their financial health is in jeopardy, they should bring an application for recovery, and provide individualized evidence demonstrating that recovery of amounts included in Account 1509 is required to maintain their viability. Even if the Board determines that an ROE deadband should be used as a threshold for an application, it should simply act as a necessary but not a sufficient condition to be eligible for recovery, and even with that, it should be far lower than 300 basis points from the utility's deemed level included in rates.

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[15] See the chart at the following link. The TSX Composite Index has lagged the performance of the S&P for 500 not just before but after the start of the pandemic.
[16] For example, Greater Sudbury Hydro Inc. secured long-term debt at a rate of 1.98% beginning March 26, 2020 (See Appendix 2-OB, included with the Settlement Proposal in EB-2019-0037), and Oshawa PUC Networks Inc. secured long-term debt starting on October 1, 2020, at a rate of 2.22%.(See Appendix 2-OB, included with the Settlement Proposal in EB-2020-0048)
[17] Staff Proposal, p.7
[18] LPMA, p.40
[19] EDA, p.4
[20] AMPCO/IGUA, para. 22

Both the OEA/CLD+ and EDA make reference to a 100 basis points deadband that the Board had adopted in certain Earning Sharing Mechanisms ("ESM") as potentially a more appropriate deadband, than the 300 basis points included in the Staff Proposal. SEC submits that this is an inappropriate comparison, as it implies a guiding principle about "sharing" the costs and reduced revenues, not ensuring utilities remain financially viable. The ESM mechanism, which is almost always asymmetrical, is as the name suggests about sharing gains in certain circumstances. Moreover, ESMs are an exception, not the norm, in rate-setting plans. They are in place for certain Custom IR plans and during deferred rebasing periods only arising from a MAADs application. In the latter situation, we note that the ESM deadband is 300, not 100 basis points.

Eligible Costs

OEA/CLD+ and Kitchener Wilmot Hydro Inc. ("KWHI") have proposed that all incremental bad debt should be treated as fully recoverable, if the upper end of the proposed Means Test is not met.[21] Notwithstanding SEC's position outlined in our initial comments that there should be no distinction between categories of costs, we think it is necessary to challenge the premise of the OEA/CLD+'s position on this issue. OEA/CLD+'s view is that this creates a financial disincentive for utilities to provide assistance to their customers at a time where they need it most, and that the beneficiary of the activity is still the customer.

The OEA/CLD+'s rationale for its position seems focused on bad debt caused by utility-initiated relief programs, yet its proposal appears to include all incremental bad debt, regardless of whether it arises due to a relief program. SEC assumes that a significant portion of incremental bad debt that utilities are incurring has nothing to do with relief programs (mandated or voluntary), but is simply caused by businesses unable to pay their bills, completely unrelated to any relief programs.

The larger premise of the OEA/CLD+'s position is that, since the relief programs are helping some customers, all of the other customers should be required to pay. SEC disagrees. There is a benefit to a utility offering a voluntary relief program. Not only does it raise the standing of the utility within the community, but in many cases it may result in less bad debt than would otherwise have been the case if the voluntary program had not been in place.

LPMA correctly points out that, with respect to government (either through emergency order or the OEB) mandated relief and other requirements, there is an assumption in the Staff Proposal that regulated utilities have been treated differently than other segments of the economy, and so it is only fair that they be able to recover 100% of these costs.[22] It is readily apparent that this is not correct. Government actions and requirements have impacted every segment of the Ontario economy, imposing both increased costs and lower revenues. LPMA's example of property owners is most apt.[23] The government has issued emergency orders during the pandemic banning evictions, which will in many cases lead to increases in their bad debt expenses. Those property owners cannot simply pass on that bad debt expense to their existing customers.

Savings

SEC is confused by the OEA/CLD+'s recommendation related to the requirement to record costs net of savings that is included in the Staff Proposal. Under the heading "measurement of achieved savings is not a necessity", OEA/CLD+ appears to recommend that the Board not include a requirement to provide evidence on savings, and not to include COVID-19 related savings as an offset to any additional costs/lost revenue, because those savings would be included within the ROE calculation used for the deadband.

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[21] OEA/CLD+, p.7; KWHI, p.2
[22] LPMA, p,.18
[23] LPMA, p.18

This is confusing two separate issues. The actual ROE will include in the normal course costs and savings, but the purpose of the calculation is to set the threshold for recovery. But for the purpose of determining the amount of recovery, based on the Staff Proposal, that must include costs net of the savings. To calculate that, the utilities will have to quantify the savings that have occurred.

More importantly, as SEC noted in our initial comments, it is not sufficient for utilities to record actual savings. Utilities should be required to file evidence that demonstrates they took appropriate actions to mitigate the financial impacts and reduce costs where it was possible. The Board should then assess whether they did as much as reasonably could be expected. If they had not, the Board should impute a level of savings that should have been achieved by a utility acting prudently.

Other Jurisdictions

OEA/CLD+ provided a report from ScottMadden[24], similar to the report filed by LEI, which is a jurisdictional scan of how other state and provincial utility regulators have treated COVID-19 costs and lost revenue. A review of the data in the ScottMadden report shows, similar to the findings of the LEI Report, that most other regulators have not yet grappled with the question that the Board is attempting to address in this consultation. At most what can be gleaned from the ScottMadden Report is that most other regulators have approved a deferral account related to at least one component of the COVID-19 pandemic on regulated utilities, but there are only a few that have actually approved any recovery. Similar to the Board, most have simply approved the recording of costs and lost revenue for consideration in a future proceeding. In fact, what stands out is that very few have reached any final determination on the issue, and of the few that have, many have denied recovery of at least some cost amounts (most notably, lost revenue for waived fees or lost load). [25]

Furthermore, review of the underlying records of some of the proceedings referenced in the ScottMadden report[26], shows that most of these decisions were made in a manner similar to what the Board did last spring. Accounting Orders were issued without a full record, and most with little if any ratepayer involvement, in the same way the Board did so in the early days of the pandemic, i.e. to ensure it would be able to address the issue in the future.

Ontario does stand out in one major respect as compared to Canadian provincial regulators. The Board is the only Canadian provincial utility regulator that has approved a generic industry wide COVID-19 impact deferral account. Most have not done anything related to tracking and recording COVID-19 impacts for the purpose of potentially allowing future recovery. In Alberta, the AUC has explicitly stated it will not create a generic account, and provided guidance for utilities who may seek to have one established.[27] As of the end of 2020, no applications have been filed[28] The only other regulators that have done anything are a) PEI, with respect to its major utility (Maritime Electric), approving a deferral account limited to tracking a subset of costs related to a certain support program, and b) the BCUC with respect to a costs and lost revenue for a district energy provider (Creative Energy).[29] There have been no deferral accounts created for any of the major BC electricity or gas utilities.[30] Across the rest of the country, utility regulators have not taken any action, and utilities have not been requesting to be provided with additional funds to deal with the impact of the pandemic.

[24] OEA/CLD+, Appendix B
[25] OEA/CLD+, Appendix B, p.28
[26] OEA/CLD+, Appendix B
[27] Alberta Utilities Commission, Ruling on the Office of the Utilities Consumer Advocate Motion, October 8, 2020 (Proceeding 25767)
[28] OEA/CLD+, Appendix B, p.48
[29] OEA/CLD+, Appendix B, p.49
[30] OEA/CLD+, Appendix B, p.48

EPCOR

EPCOR Natural Gas LP ("EPCOR") focused its comments on what it believed were the unique circumstances of its Southern Bruce operations, which in its view entitle it to recovery of 100% of its incremental costs resulting from the COVID-19 pandemic. EPCOR's view is that its Southern Bruce service territory is operating under a unique 10-year rate stability period that arose out of the competitive process in EB-2016-0137/0138/0137, and this somehow makes it different from other utilities.

SEC submits that EPCOR has not taken on any more or less risk that any other utility has, under whatever rate-setting framework, related to the impacts of a once in a century global pandemic. The fact that EPCOR's rates are set in a particular manner does not make their risk greater than other utilities. The rate stability period was a requirement under competitive processes that awarded EPCOR the right to construct a natural gas distribution system in Southern Bruce. It was there to ensure fairness to both proponents, and involved assuming specific risks related to attachment forecast and construction costs during this period. While that rate-setting framework includes a Z-Factor, so does the framework in place for all other utilities. The Staff Proposal is correct in saying that the COVID-19 pandemic is not a Z-Factor, and so a different mechanism is required to determine if, and to what extent, recovery of amounts to augment existing rates is required.

SEC therefore submits that EPCOR's situation is, from the point of view of this consultation, no different from any utility that is already up and running.

The Situation Continues to Evolve

SEC does agree with the OEA/CLD+, EDA and others that the COVID-19 pandemic is unfortunately far from being over, and the impacts on utilities and their customers will undoubtedly change over time.[31] It perhaps goes without saying that the Board should keep that in mind in crafting a policy, and also should recognize that it may need to consider changes over time, if and when the circumstances warrant.

It will be up to individual Board panels, seized with specific applications for recovery, to scrutinize the evidence in those proceedings on the impact of the COVID-19 pandemic on the utility before them, but also on the customers in that utility's service territory. SEC's comments are intended to ensure that those individual Board panels have principles and guidelines arising out of this consultation, but they are not fettered by a mechanistic or overly prescriptive approach to the applications they are hearing.

All of which is respectfully submitted.

Yours very truly,
Shepherd Rubenstein P.C.

Mark Rubenstein

cc: Wayne McNally, SEC (by email)
Interested Stakeholders (by email)

[31] OEA/CLD+, p.4, EDA, p.14