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**BY EMAIL**

November 1, 2024

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Ontario Energy Board  
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Dear Ms. Marconi:

**Re: Ontario Energy Board (OEB) Staff Submission  
Burlington Hydro Inc. (Burlington Hydro)  
Application for 2025 Rates  
OEB File Number: EB-2024-0010**

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Please find attached OEB staff's submission in the above referenced proceeding, pursuant to Procedural Order No.1.

Yours truly,

Yaroslav Paliy  
Advisor, Generation & Transmission

Encl.

cc: All parties in EB-2024-0010



# **ONTARIO ENERGY BOARD**

## **OEB Staff Submission**

**Burlington Hydro Inc.**

**Application for 2025 Rates**

**EB-2024-0010**

**November 1, 2024**

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## Introduction

Burlington Hydro Inc. (Burlington Hydro) filed an incentive rate-setting mechanism (IRM) application with the Ontario Energy Board (OEB) on August 15, 2024, under section 78 of the *Ontario Energy Board Act, 1998* seeking approval for changes to its electricity distribution rates to be effective January 1, 2025. Burlington Hydro's application is based on a Price Cap Incentive Rate-setting (Price Cap IR) option.

Consistent with Chapter 3 of the OEB's *Filing Requirements for Electricity Distribution Rate Applications*, Burlington Hydro applied the Price Cap IR adjustment factor to adjust the monthly service charge and distribution volumetric rate during the incentive rate-setting years. An inflation factor of 3.60% applies to all IRM applications for the 2025 rate year.<sup>1</sup> The stretch factor assigned to Burlington Hydro is 0.15%,<sup>2</sup> resulting in a rate adjustment of 3.45% based on the Price Cap adjustment formula. OEB staff has no concerns with Burlington Hydro's proposed price cap adjustment.

Burlington Hydro has also requested approval for:

1. Updating the Retail Transmission Service Rates (RTSRs)
2. Disposition of Group 1 Deferral and Variance Account (DVA) balances
3. Rate riders for 2025 LRAM-eligible amounts
4. Incremental Capital Module (ICM) funding

OEB staff has no concerns with Burlington Hydro's requests regarding the RTSRs, disposition of Group 1 DVA balances, or rate riders for 2025 LRAM-eligible amounts. In this document, OEB staff has made detailed submissions below on the ICM funding request.

## Incremental Capital Module (ICM)

### Background

Burlington Hydro has requested \$5,120,792 in ICM funding for the mandatory relocation of electrical distribution assets required for road widening work on Dundas Street (from Guelph Line to Kerns Road and from Northampton Boulevard to Guelph Line). The relocation work was requested by the Regional Municipality of Halton (Halton Region), the road authority under the *Public Service Works on Highways Act* (PSWHA).

Burlington Hydro states that it must relocate approximately 164 poles (and associated hardware, cable and wire) and 21 transformers. The scope includes the installation of

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<sup>1</sup> OEB Letter, 2025 Inflation Parameters, issued June 20, 2024

<sup>2</sup> Empirical Research in Support of Incentive Rate-Setting: 2023 Benchmarking Update, Report to the Ontario Energy Board, July 2024, p. 23, Table 5

new poles, the transfer of conductors to the new poles, the removal of old poles in the overhead portion, and the relocation/installation of underground infrastructure.

Burlington Hydro states that for road authority relocation requests, it follows the PSWHA and associated regulations and collects contributed capital of 50% of the labour and labour-saving equipment (i.e., vehicles). Halton Region will provide \$4,515,403 in contributed capital for this project.

The total incremental annual revenue requirement associated with the ICM request is \$151,229. Burlington Hydro proposes recovery of the incremental annual revenue requirement through ICM rate riders effective January 1, 2025 to December 31, 2025. The revenue requirement for the Residential class will be recovered via a fixed rate rider, while rate riders for all other classes will be based on current fixed and variable revenue proportions.

The expected start date of the project is January 1, 2025, and the in-service date is December 31, 2025.

## OEB Staff Submission

In making its submission on the 2025 ICM funding request, OEB staff considered the OEB's established criteria for ICM funding set out in the *Report of the Board - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module* (the ACM Report)<sup>3</sup>. These criteria are materiality, need, and prudence.<sup>4</sup>

OEB staff supports Burlington Hydro's request for ICM funding, however, OEB staff are concerned that ICM amounts are not fully outside of the base upon which rates were derived, and that not all amounts to be incurred are prudent. As a result, OEB staff submits that the total requested incremental capital amount of \$5,120,792 should be reduced by 7% or \$358,449

A breakdown of how Burlington Hydro's application relates to each criterion in the ACM Report is found in the subsequent sections below.

## Materiality

There are three elements to the materiality criterion. The application must first meet the materiality threshold, which determines a distributor's maximum eligible capital funding. Second, the distributor must demonstrate that the project is not a minor expenditure in

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<sup>3</sup> Report of the Board - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014

<sup>4</sup> *Ibid.*, p. 16

comparison to the overall capital budget. Finally, the incremental funding must have a significant influence on the operation of the distributor.

### **Materiality Threshold**

The OEB uses the materiality threshold formula which considers both the growth of the utility and the inflationary increase since the last rebasing year<sup>5</sup>, to determine the maximum eligible incremental capital amount.<sup>6</sup> The following equation is used by the OEB to calculate the materiality threshold:

$$\text{Threshold Value}(\%) = \left( 1 + \left[ \left( \frac{RB}{d} \right) \times (g + PCI \times (1 + g)) \right] \right) \times ((1 + g) \times (1 + PCI))^{n-1} + X\%$$

Where:  $n$  = number of years since cost-of-service rebasing

$RB$  = Rate Base included in base rates (\$)

$d$  = depreciation expense included in base rates (\$)

$g$  = distribution revenue change from load growth (%)

$PCI$  = price cap index

$X$  = dead band of 10%

The Price Cap Index (PCI) to be used in the above formula is the Input Price Index (IPI) less the stretch factor of 0.3. The inflationary factor or IPI to be used according to the ICM policy is the IPI from the utility's most recent Price Cap IR application. The growth factor should be calculated based on the percentage difference in distribution revenues between the distribution revenues from the most recent complete year and the distribution revenues from the most recent approved test year.

Burlington Hydro used the OEB-approved materiality threshold formula to arrive at a threshold capital expenditure value of \$11,771,200. Burlington Hydro's 2025 capital forecast is \$16,891,993. The total net cost of the project, not including capital contributions, is \$5,563,693. Based on the 2025 capital forecast and the calculated materiality threshold, the maximum eligible incremental capital amount is \$5,120,792.

OEB staff submits that Burlington Hydro's 2025 capital forecast exceeds the materiality threshold calculated using the OEB-approved materiality threshold formula and acknowledges that Burlington Hydro is requesting to recover only the maximum eligible

<sup>5</sup> Burlington Hydro last rebased in 2021 (EB-2020-0007)

<sup>6</sup> *Filing Requirements for Electricity Distribution Rate Applications – Chapter 3 Incentive Rate-Setting Applications*, June 18, 2024

incremental capital amount of \$5,120,792.

### ***Project-Specific Materiality Threshold***

The ACM Report addressed the project-specific materiality threshold criterion as follows:

Minor expenditures in comparison to the overall capital budget should be considered ineligible for ACM or ICM treatment. A certain degree of project expenditure over and above the Board-defined threshold calculation is expected to be absorbed within the total capital budget.<sup>7</sup>

Burlington Hydro states that the ICM project is material on a project-specific basis. The project is equal to 33% of Burlington Hydro's total 2025 capital expenditure forecast of \$16,891,993.

OEB staff submits that Burlington Hydro's ICM project constitutes a significant portion of its overall capital expenditure forecast and therefore, in OEB staff's view, satisfies the project-specific materiality threshold.

### ***Significant Influence on Operations***

The ACM Report states that any amount being requested for ICM funding must clearly have a significant influence on the operation of a distributor. Burlington Hydro states that the road widening project makes up a significant portion of its total capital expenditure forecast and will have a significant influence on company operations.

OEB staff submits that this project will have a significant influence on company operations given the size of the financial expenditure.

### **Need**

The ACM Report describes the "need" criterion as follows:

The distributor must pass the Means Test (as defined in the ACM Report).

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<sup>7</sup> Report of the OEB - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014

Amounts must be based on discrete projects and should be directly related to the claimed driver. The amounts must be clearly outside of the base upon which the rates were derived.<sup>8</sup>

### ***Means Test***

Under the Means Test, if a distributor's regulated return on equity (ROE) exceeds 300 basis points above the deemed ROE embedded in the distributor's rates, then the funding for any incremental capital project will not be allowed.<sup>9</sup> Burlington Hydro stated that its 2023 actual ROE was 8.11%, which is 0.23% (23 basis points) lower than its deemed ROE of 8.34%.

OEB staff submits that Burlington Hydro has not exceeded its deemed rate of return by 300 basis points and, therefore, passes the Means Test for the 2025 ICM.

### ***Discrete Project***

The ACM Report indicates that incremental capital funding is for discrete projects and not for ongoing capital programs. Burlington Hydro states that relocation project is a distinct, non-discretionary System Access project, and is unrelated to Burlington Hydro's recurring annual capital projects.

OEB staff submits that the proposed ICM project is discrete and is not related to ongoing capital programs.

### ***Directly Related to the Claimed Driver***

Burlington Hydro states that the driver of this project is a mandatory request by Halton Region to accommodate the Dundas Street Road Widening Project (Guelph Line West to Kerns Road and Guelph Line East to Northampton Boulevard). The project involves relocating Burlington Hydro's electrical distribution assets on Dundas Street to comply with the request.

OEB staff submits that the incremental capital request for relocating distribution assets directly relates to the claimed drivers identified by Burlington Hydro.

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<sup>8</sup> Report of the OEB - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014, p. 17

<sup>9</sup> *Ibid.*, p. 15



### ***Outside of Base Upon Which Rates Were Derived***

OEB staff submits that the ICM amounts are not fully outside of the base upon which rates were derived. As a result, OEB staff submits that the OEB should reduce the ICM amount for the reasons that follow.

Given the extended period between the ICM request and when rates were last derived, OEB staff believes it is appropriate to evaluate what constitutes a normal level of capital expenditure for pole and transformer replacement included in base rates by looking at asset condition.

OEB staff and the Vulnerable Energy Consumers Coalition (VECC)<sup>10</sup> asked Burlington Hydro to provide the age and condition of the 164 poles (and associated hardware, cable and wire) and the 21 transformers that must be relocated.<sup>11</sup> Burlington Hydro provided a response and identified that four poles and one transformer are in Poor condition.<sup>12</sup>

Burlington Hydro provided an estimated cost per pole and per transformer replaced as part of its reply to interrogatory Staff-15. The estimated cost per pole and per transformer replaced is \$38,754 and \$42,741, respectively. OEB staff believes that the four poles and one transformer in Poor condition would be expected to be replaced in the near-term and should be accounted for as part of base rates in Burlington Hydro's 2021 Distribution System Plan. OEB staff notes that a similar approach was taken by the OEB in a Z-factor application<sup>13</sup> for Elexicon Energy Inc. (Elexicon Energy). In the application, Elexicon Energy sought recovery of \$4,602,788 in expenditures associated with the restoration of electricity service to its customers following the May 21, 2022 derecho storm event. In its submission, OEB staff noted that Elexicon Energy incurred material costs to restore electricity service as a result of the derecho storm, and that the claimed costs largely satisfied the causation and prudence criteria for Z-factor recovery. However, OEB staff submitted that a portion of the costs included in the Z-factor claim for replacement of damaged poles that were in Poor and Fair-Poor condition should be disallowed.<sup>14</sup> OEB staff argued that pole replacement costs associated with the Poor and Fair-Poor condition poles be disallowed as such costs should have been accounted for in Elexicon Energy's pole renewal program outlined in its 2021 Distribution System Plan.<sup>15</sup>

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<sup>10</sup> An approved intervenor in this proceeding

<sup>11</sup> OEB Staff Interrogatories, Staff-17, October 4, 2024

<sup>12</sup> Burlington Hydro Interrogatory Response to Staff-17 and VECC-7, October 18, 2024

<sup>13</sup> EB-2022-0317

<sup>14</sup> EB-2022-0317, OEB Staff Submission, April 6, 2023, p. 1

<sup>15</sup> *Ibid.*, p. 8

In its Decision and Order in the Z-factor application, the OEB reduced Elexicon Energy’s Z-factor cost claim in the Poles and Overhead Conductor category by 12% (or \$322,000) on the basis that the poles classified as Poor and Fair-Poor would have been replaced within one to two years.<sup>16</sup> Although this precedent was for a Z-factor cost claim, OEB staff submits that a similar approach is appropriate in the case of Burlington Hydro’s ICM request. OEB staff submits that the OEB should reduce the ICM amount by at least \$197,757 (approximately 4%) – the estimated value of replacing the four poles and one transformer denoted to be in Poor condition. The ICM reduction of \$197,757 is calculated in Table 1 below:

**Table 1: ICM Reduction for Poles and Transformer in Poor Condition<sup>17</sup>**

Four Poles at \$38,754	\$155,016
One Transformer at \$42,741	\$42,741
<b>ICM Reduction</b>	<b>\$197,757</b>

## Prudence

The ACM Report describes the “prudence” criterion as follows:

The amounts to be incurred must be prudent. This means that the distributor’s decision to incur the amounts must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.<sup>18</sup>

Based on Burlington Hydro’s evidence, OEB staff submits that not all amounts to be incurred are prudent.

Burlington Hydro states that the project represents prudent investments and delivers the most cost-effective option for customers based on an assessment of alternatives. Burlington Hydro considered three project alternatives: status quo, like for like, and upgrade. Status quo was not an option as it would be in direct violation of the PSWHA. Like for like was not considered as it would not be in compliance with mandatory standards and regulations. OEB staff acknowledges Burlington Hydro’s consideration of alternatives.

<sup>16</sup> EB-2022-0317, Decision and Order, June 15, 2023, p. 12

<sup>17</sup> Burlington Hydro Interrogatory Response to Staff-15, October 18, 2024

<sup>18</sup> Report of the OEB - New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, September 18, 2014, p. 17

Burlington Hydro states that it arrived at the cost estimate of the project based on the road widening design from Halton Region and according to O. Reg. 22/04, Canadian Standards Association standards, and Burlington Hydro standards and specifications. Material costs were estimated by referencing the bill of materials from the utility relocation design and Burlington Hydro's most recent purchase prices. Burlington Hydro obtained a quote for the labour and equipment costs from a contractor who had successfully completed a relocation project for the utility in the past. Burlington Hydro also noted that it expects the actual costs for this project to be within 75-125% of the estimate.<sup>19</sup> However, OEB staff is concerned with the cost estimate provided by Burlington Hydro for the reasons that follow.

Burlington Hydro provided an estimated cost per pole replaced and per transformer replaced for the requested ICM project (2025 Dundas St Road Widening) and a comparable 2021 Waterdown Road Widening project as shown in Table 2 below<sup>20</sup>:

**Table 2: Estimate Cost Per Unit Replaced**

Project	Cost per Pole	Cost per Transformer	Cost per km of Underground Cable
2025 Dundas St Road Widening	\$38,754	\$42,741	\$381,008
Waterdown Road Widening	\$28,291	\$12,062	\$362,712
Variance (\$)	\$10,463	\$30,678	\$18,296

The requested ICM project has significantly higher costs than the comparable project for cost per pole (37% higher), transformer (254% higher), and underground cable (5% higher) replaced. Burlington Hydro stated that the higher estimated unit costs for this project are driven by the type of assets to be replaced, the road widening design which incorporates upgrades to meet current standards and inflationary increases for materials, labour, and equipment. While OEB staff agrees that each relocation project is unique, with varying design and scope differences that inherently affect the costs, OEB staff cannot ignore the 254% increase in cost per transformer replaced when compared to the Waterdown Road Widening project.

OEB staff provides the following tables to account for the inflationary increases from 2021 to 2025 based on the Waterdown Road Widening project cost per transformer replaced of \$12,062. Table 3 inflates the cost per transformer based on the OEB-

<sup>19</sup> Burlington Hydro Interrogatory Response to Staff-15, October 18, 2024

<sup>20</sup> *Ibid.*

approved inflation parameters, while Table 4 inflates the cost per transformer based on the Statistics Canada Power, Distribution and Other Transformers Price Index<sup>21</sup>.

**Table 3: OEB-approved Inflation Parameter**

Year	Inflation	Cost per Transformer
2021		\$12,062.00
2022	3.30%	\$12,460.05
2023	3.70%	\$12,921.07
2024	4.80%	\$13,541.28
2025	3.60%	<b>\$14,028.76</b>

**Table 4: Statistics Canada Power, Distribution and Other Transformers Price Index**

Year	Quarter	Index	Change	Cost per Transformer
2021	Q1	106.1		\$12,062.00
	Q2	104.6	-1.4%	\$11,891.47
	Q3	110.1	5.3%	\$12,516.74
	Q4	121.1	10.0%	\$13,767.28
2022	Q1	125.5	3.6%	\$14,267.49
	Q2	138.9	10.7%	\$15,790.87
	Q3	145.4	4.7%	\$16,529.83
	Q4	152.3	4.7%	\$17,314.26
2023	Q1	158.6	4.1%	\$18,030.47
	Q2	159.1	0.3%	\$18,087.32
	Q3	159	-0.1%	\$18,075.95
	Q4	157.9	-0.7%	\$17,950.89
2024	Q1	169.5	7.3%	\$19,269.64
	Q2	169.5	0.0%	<b>\$19,269.64</b>

The cost per transformer identified for the ICM project which Burlington Hydro is requesting funding, as per Table 2 above, is 205% higher than the inflated cost calculated in Table 3 and 195% higher than the inflated cost calculated in Table 4.

Even after accounting for the higher levels of inflation (i.e., the Statistics Canada data in Table 4), costs per transformer replaced for the ICM project are still substantially higher than the comparable project. Furthermore, Burlington Hydro indicated that it obtained a quote for the labour and equipment costs from a contractor who had successfully

<sup>21</sup> <https://www150.statcan.gc.ca/>

completed a relocation project for the utility in the past (i.e., the estimated labour and equipment costs are solely based on a quote from one contractor and do not reflect a competitive procurement process). OEB staff submits that the OEB should reduce the cost per transformer replaced from \$42,741, as seen in Table 2, to \$35,089. This reduced cost per transformer replaced will be closer to the costs calculated in Tables 3 and 4, while still acknowledging that each relocation project is unique with varying design and scope differences that inherently affect the costs. This will further reduce the requested ICM amount by \$160,692 (approximately 3%) to reflect the lack of prudence in the cost estimate process and the resulting requested costs. Please see Table 5 below for a calculation of the ICM funding reduction related to the reduction of costs per transformer replaced.

**Table 5: Proposed Reduction of Costs per Transformer Replaced**

	<b># of Transformers to be Replaced</b>	<b>Cost per Transformer</b>	<b>Total Cost</b>
Requested	21	\$42,741	\$897,561
Proposed Reduction	21	\$35,089	\$736,869
Total Reduction			<b>\$160,692</b>

In total, combining the proposed reduction in transformer costs with OEB staff's reduction of \$197,757 associated with the four poles and one transformer denoted as Poor condition, OEB staff submits that a total reduction of \$358,449 should be made to Burlington Hydro's ICM funding request.

~All of which is respectfully submitted~