



BY EMAIL AND WEB POSTING

June 16, 2020

To: All Rate-regulated Entities and Interested Parties

Re: 2020 Q3 Prescribed Interest Rates

The Ontario Energy Board (OEB) is issuing this letter to set the 2020 Q3 prescribed interest rates for Deferral and Variance Accounts (DVAs) at 1.38% and Construction Work in Progress (CWIP) at 2.48%. In this letter, the OEB is also providing a rationale as to why the approach to set the 2020 Q3 DVA prescribed interest rate departs from the [OEB's Approved Prescribed Interest Rates Methodology](#).

The OEB's Approved Prescribed Interest Rates Methodology

In a letter issued to all rate-regulated electricity distributors and natural gas utilities dated November 28 2006, the OEB approved a prescribed interest rates methodology:¹

- Prescribed Interest Rate for DVAs: the quarterly calculated interest rate equals to the three-month bankers' acceptance rate, plus a fixed spread of 25 basis points²
- Prescribed Interest Rate for CWIP: the quarterly calculated interest rate equal to FTSE Canada Mid-term Bond Index - All Corporate³

¹ EB-2006-0117, OEB's Letter Re "Approval of Accounting Interest Rates Methodology for Regulatory Accounts Board File No. EB-2006-0117", November 28, 2006.

² In January 2019, the Investment Industry Regulatory Organization of Canada began publishing transaction-based one- and three-month Bankers' Acceptance (BA) rates. These rates are published on a delayed basis for informational purposes only and replace the BA rates formerly published on the Bank of Canada website.

³ In the OEB's 2006 letter, the data source referenced was the Scotia Capital Inc. All Corporates Mid-Term Average Weighted Yield. This index is unchanged but is now calculated by a separate financial data

The OEB stated in the letter that “These two prescribed rates will be reviewed each quarter and updated if the change is 25 or more basis points”. The letter also provided the timing of the interest rates calculation: the referenced rates as at month end, one month prior to the start of the quarter.

2020 Q3 Prescribed Interest Rates

Using the OEB’s approved methodology, the 2020 Q3 prescribed interest rate for CWIP remains unchanged from Q2 at 2.48%, as the change between the calculated Q3 interest rate of 2.62% (which is the mid-term bond index as at May 29, 2020) and the approved Q2 interest rate of 2.48% is less than 25 basis points.

During the unprecedented state of emergency arising from the COVID-19 pandemic, the referenced rate for the DVA prescribed interest rate, i.e. the three-month Bankers’ Acceptance rate, has been declining sharply since late March 2020, in line with the reductions in the Bank of Canada’s key overnight rate. As the COVID-19 pandemic was emerging in Europe and North America, the Bank of Canada and other central banks reduced key rates precipitously.⁴ Three-month Canadian Corporate bond yields for AA-rated, A-rated and BBB-rated corporations have also shown volatility. There was a spike in late March following the announcements of the states of emergency in North America. While rates have declined since then, there continues to be volatility through to the end of May, as summarized in the following table:⁵

Date Range	Sep. 2019 – mid. Jan. 2020	Late Jan. 2020 – Feb. 2020	2 nd week March 2020 (collapse)	Late March 2020 (spike)	April 2020	May 2020
BBB-rated	2.1% to 2.25%	2.0%	Steep decline to 1.4%	Sharp spike to 3.25%	Sharp decline to about 2.1%	Further decline and volatility to about 1.64%
A-rated	2.0% to 2.1%	1.85% to 1.9%	Steep decline to 1.22%	Sharp spike to 2.65%	Sharp decline to 1.3%	Further gradual decline to 1.14%
AA-rated	1.8% to 2.0%	1.6% to 1.8%	Steep decline to 1.175%	Sharp spike to 2.65%	Sharp decline to 1.15%	Gradual decline and volatility in late May between 0.9% and 0.55%

service provider on a commercial basis. The OEB, under contract, obtains this yield rate from PC Bond Analytics, a business unit of FTSE.

⁴The Bank of Canada reduced its policy interest rate, then set at 1.75%, by 50 basis points on March 4, 2020. This was followed by two unprecedented emergency announcements of further reductions of 50 basis points each on March 16, 2020 and March 27, 2020. The key rate now sits at 0.25%.

⁵ Source: Bloomberg LP

With a view to maintaining stability for the interest rates, the OEB has determined that 2020 Q3 prescribed interest rate for DVAs will be updated to 1.38%. This is calculated as the average of the Q2 interest rate of 2.18% and the calculated Q3 interest rate of 0.57% calculated with the OEB's approved methodology.⁶ Using the average of the two rates smooths the impact during this unprecedented time and aligns with the average of AA-, A- and BBB- rated Canadian Corporate bond yields since the middle of May, 2020.

Next Steps

The OEB will continue monitoring the market conditions. Stakeholders may provide comments on factors the OEB should consider when setting the interest rates for 2020 Q4. Any comments, suggestions and questions relating to this letter should be directed to the OEB's Industry Relations Enquiry e-mail at IndustryRelations@oeb.ca. Please include "2020 Q4 Prescribed Interest Rates" in the subject line.

Yours truly,

Original Signed By

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⁶0.57% is calculated as the three-month bankers' acceptance rate as at May 29, 2020 of 0.32% plus the 0.25% spread.