ONTARIO ENERGY BOARD | COMMISSION DE L'ÉNERGIE DE L'ONTARIO

BACKGROUNDER

DECISION AND ORDER - EB-2022-0028
EPCOR ELECTRICITY DISTRIBUTION ONTARIO INC.
June 19, 2023

June 19, 2023

Ontario Energy Board issues decision on EPCOR Electricity Distribution's 2023 major rates application

DECISION

On June 15, 2023, the Ontario Energy Board (OEB) issued its Decision and Order on an application filed by EPCOR Electricity Distribution Ontario Inc. (EPCOR Distribution) for approval to change its electricity distribution rates effective October 1, 2023.

The application was the subject of settlement negotiations between EPCOR Distribution and intervenors representing a variety of customer classes. These negotiations resulted in a partial settlement that was reviewed and accepted[1] by the OEB on December 20, 2022. The OEB held an oral hearing on February 14-15, 2023 on the remaining issues.

The Decision and Order issued June 15, 2023 relates to those remaining issues.

Overall, the OEB found that EPCOR Distribution's forecasts for capital expenditures and operating, maintenance and administration (OM&A) costs were not fully justified on the evidence provided. Accordingly, the OEB determined that a reduction of $500,000 in relation to capital expenditures (from $4.3 million to $3.8 million) and of $700,000 in relation to OM&A (from $6.53 million to $5.83 million) is necessary to establish just and reasonable rates.

EPCOR Distribution's new rates will take effect as of October 1, 2023. Starting May 1, 2024, and January 1 in the three subsequent years, EPCOR Distribution may apply to have its rates adjusted using an OEB-approved mechanism that accounts for inflation and productivity.

The bill impacts for EPCOR Distribution's customers will be known later this summer when the OEB approves a rate order that reflects the Decision and Order.

BACKGROUND

EPCOR Distribution serves about 19,000 customers in Collingwood, Stayner, Creemore (part of Clearview Township) and Thornbury (part of the Town of the Blue Mountains). It was formed October 1, 2018 following the OEB's[2] approval of two share purchase transactions that would result in EPCOR Collingwood Distribution Corporation becoming the new owner of Collus PowerStream Corporation (since renamed EPCOR Distribution).

EPCOR Distribution filed a cost-based application seeking OEB approval to change the rates that it charges to distribute electricity to its customers. Initially, EPCOR Distribution applied for new rates effective January 1,

[1] Procedural Order No. 5, December 20, 2022
[2] EB-2017-0373, August 18, 2018

2023. EPCOR Distribution subsequently amended its application seeking an effective date of October 1, 2023, in keeping with the commitment it made when acquiring the utility in 2018.

A settlement conference was held as part of this proceeding and resulted in a partial settlement that was reviewed and accepted by the OEB.

Intervenors in the proceeding were:

- Environmental Defence Canada Inc.
- School Energy Coalition (SEC)
- Small Business Utility Alliance
- Vulnerable Energy Consumers Coalition (VECC)

KEY FEATURES

Mergers, Amalgamations, Acquisitions and Divestitures (MAADs) Proceeding *(Section 4.1, pp. 5-8)*

The MAADs proceeding was considered given the difference between the capital and OM&A costs that were forecast at the time and EPCOR Distribution's actual spending as set out in its rate application.

The evidence before the OEB in the MAADs proceeding included forecasts that predicted savings resulting from efficiencies that would be achieved by the new owner. While the decision in that proceeding did not expressly make those predicted savings a binding commitment, they were an indication of what the applicant, a professional utility manager, thought could be achieved, and they provide context to measure what EPCOR Distribution actually achieved in the five years since it took over management of the utility.

There was no evidence that the utility was troubled by chronic undercapitalization, falling reliability, persistent safety infractions or persevering customer complaints prior to the acquisition by EPCOR Distribution.

In the MAADs proceeding, the OEB was satisfied that the acquisition of the utility would not result in harm to ratepayers, based on the forecasts provided at that time. Having reviewed the actual results presented in this proceeding against the forecasts provided in the MAADs proceeding, it appears that the forecast savings did not materialize and that the utility's performance on certain system reliability indicators (SAIDI and SAIFI) has worsened.

The OEB used this opportunity to note that unrealistic forecasts can undermine the objectives of the MAADs process.

Test Year Capital Expenditures *(Section 4.2.2, pp. 8-13)*

The OEB found that EPCOR Distribution has not established the need for the proposed $4.3 million capital budget for the Test Year. The OEB agreed with the intervenors and OEB staff that the 2023 Test Year capital budget can be reduced by $500,000 based on the following considerations:

- EPCOR Distribution had higher than forecast expenditures since it acquired the utility, but it has not demonstrated that those higher levels of spending continue to be needed.
- EPCOR Distribution can better manage the pacing and level of proposed capital expenditures over the next five years starting with a lower budget than the proposed 2023 Test Year capital budget.
- There is insufficient justification for the proposed pace of pole replacements due to the limited data available on the condition of existing poles.

- The amount proposed for road authority[3] work (typically involving relocations of electricity infrastructure at the request of road authorities) is higher than historical expenditures and the increase is solely and insufficiently supported on the basis of conversations with municipal staff about potential road projects.

The OEB noted that over the coming five years, EPCOR Distribution will have an incentive to manage the pacing of its capital expenditures, including its pole replacement program.

OM&A *(Section 4.3, pp. 13-23)*

The OEB found that EPCOR Distribution has not established the need for the proposed $6.53 million OM&A budget for the Test Year.

In addition to noting that the savings that were forecast in the MAADs proceeding did not appear to have materialized, the OEB noted that the Test Year OM&A costs appear to be higher than what one would expect if the acquisition had not occurred. This is borne out by the analyses presented in the submissions made by SEC, VECC and OEB staff. Approving the OM&A budget as requested by EPCOR Distribution would decrease the incentive to achieve the savings that were originally identified and impose harm to the ratepayers as a result of the acquisition.

Also of concern is the level of cost resulting from services provided to EPCOR Distribution by affiliates. EPCOR Distribution's evidence does not establish a clear cost/benefit analysis, nor does it establish that those affiliates that provide services to EPCOR Distribution and other affiliated utility operations are themselves operating efficiently. If ratepayers are expected to bear the cost of those shared services, that cost must be limited to services that are actually required by EPCOR Distribution's ratepayers and only to the extent those services are used. EPCOR Distribution has not established this, given that EPCOR Distribution receives bundled services on the same basis as other EPCOR utility operations.

The intervenors and OEB staff proposed a range of reductions to the proposed OM&A budget. The OEB concluded that $700,000 is an appropriate reduction that balances the need to drive efficiency while maintaining safe and reliable service.

Effective Date *(Section 4.7, pp. 37-40)*

EPCOR Distribution amended its rate application to ask for new rates effective October 1, 2023 and to have those rates adjusted using the incentive rate mechanism (IRM) starting January 1, 2024 and annually on January 1 after that.

The OEB found that EPCOR Distribution's proposal to establish new rates effective October 1, 2023, followed by another rate adjustment three months later through an IRM application, is not reasonable.

The OEB will allow EPCOR Distribution to file for its first IRM adjustment for rates effective May 1, 2024, and not January 1, 2024. EPCOR Distribution may then apply for IRM adjustments effective January 1 for subsequent years of the IRM period.

REGULATORY TERMS

The following is a list of some of the commonly used regulatory terms that appear in this backgrounder, along with a plain language description for each.

[3] The term "road authority" refers to an entity or organization responsible for the construction, improvement, alteration, maintenance, and repair of a highway. This includes the Ministry of Transportation, municipal corporations, boards, commissions, or any other body that has control over the activities.

Cost-based application – A utility typically files a cost-based application with the OEB to reset its rates every five years based on an in-depth review of the utility's costs to serve its customers, and to invest in and maintain its distribution system. This is also referred to as "rebasing."

A "cost-based" application could be filed under either the Price Cap Incentive Rates or Custom Incentive Rates rate-setting options.

The OEB examines the utility's forecast of costs, expected number of customers to be served and the total amount of electricity to be delivered to them. *

The OEB determines the utility's revenue requirement and sets the distribution rates that the utility charges its customers to recover the cost of serving them plus the opportunity to earn a fair return.

*Distribution rates do not cover the cost of the electricity supplied to customers.

Rates that utilities charge their customers for the electricity that they use are set by the OEB separately.

Incentive regulation (also referred to as an Incentive Regulation Mechanism or "IRM") is a method of setting rates that encourages utilities to become more efficient in ways that will benefit their customers through better service and lower rate increases. The shareholders of the utilities also have the opportunity to benefit from higher earnings through efficiency improvements.

Electricity distributors typically file a cost-based application with the OEB to reset their rates every five years based on an in-depth review of their costs to serve their customers and to invest in and maintain their distribution systems. This is also referred to as "rebasing."

In each year between cost-based applications, the utility's rates are typically adjusted through the OEB-approved IRM mechanism which accounts for inflation and the OEB's assessment of productivity in the sector and efficiency improvements expected of the utility**.**

Revenue requirement is the total annual cost for a utility to provide service to its customers. It includes the cost of salaries, equipment, capital projects depreciation, taxes, interest and a return on equity.

The OEB approves a utility's revenue requirement when it decides a cost-based application and uses it to set rates that the utility can charge its customers.

Settlement conference – The purpose of a settlement conference is for the applicant and intervenors to try and settle (reach agreement on) as many issues as possible, other than any issues that the OEB has indicated should not be settled and should proceed to hearing.

Settlement negotiations are confidential.

Commissioners do not participate in a settlement conference and are not advised of the discussions that take place in the settlement conference.

Where the parties reach agreement, a settlement proposal is filed by the applicant for approval by the OEB.

System reliability – The OEB requires electricity distributors to track and report annually on how often electricity service to their customers is interrupted. Each distributor's performance on the two following system reliability indicators is reported on its OEB-mandated scorecard:

- **SAIDI =** System Average Interruption Duration Index. This is the average number of hours that power to a customer is interrupted.
- **SAIFI =** System Average Interruption Frequency Index. This is the average number of times that power to a customer is interrupted.

Test year – In a cost-based proceeding, the OEB sets rates based on the utility’s forecast of what it will cost to serve its customers.

Those forecasts are typically done for the year the proposed new rates will take effect. This will usually be the year after the application is filed and is referred to as the “test year.”

About the OEB

The OEB is the independent regulator of Ontario’s electricity and natural gas sectors. It protects the interests of consumers and supports the collective advancement of the people of Ontario. Its goal is to deliver public value through prudent regulation and independent adjudicative decision-making which contributes to Ontario’s economic, social and environmental development.

Contact Us

Media Inquiries
Phone: 416-544-5171
Email: oebmedia@oeb.ca

Consumer Inquiries
416-314-2455/1-877-632-2727

Ce document est aussi disponible en français.

This Backgrounder was prepared by OEB staff to inform Ontario’s energy consumers about the OEB’s decision and is not for use in legal or regulatory proceedings. It is not part of the OEB’s reasons for decision; those may be found in the Decision and Order issued June 15, 2023, which is the official OEB document.