

## 2023 GRA SPEAKING NOTES

### Negotiated Settlement

To facilitate my discussion of the negotiated settlement, I would like to refer to **Exhibit M-14**, which is the letter that explained those elements of the GRA that were changed as a result of the negotiated settlement.

As I walk through this letter:

- I will discuss each of the items in Table 1 that resulted in a net decrease in revenue requirement;
- I will discuss the rate riders that needed to be updated;
- And I will discuss the Weather Normalization deferral account.

### Revenue Requirement Impact

I would like to begin with **Table 1**, which highlights that the negotiated settlement results in a decrease of \$5.8 million in the revenue requirement to be collected from customers over the 3-year rate-setting period. *[which is the sum of these 7 numbers]*

- Of that \$5.8 million decrease, 62% is due to the lower ROE,
- 27% is due to a revised Provincial debt repayment schedule from the PEI Energy Corporation,
- and the remaining 11% (or \$670K net decrease) is either directly related to the first two changes and/or due to a two-month shift in the effective date of new rates (from March 1 to May 1).

In the settlement letter, I choose to focus on the impact to revenue requirement because it is the foundation that determines customers' rates. Taking a very simplistic view, a customer rate is the revenue requirement divided by the forecast annual energy sales for that group of customers. So, beneath the approval of customer rates is the approval of the revenue requirement and forecast energy sales.

## **ROE – Table 2**

- Maritime Electric's cost of capital expert, Concentric Energy Advisors, provided evidence for this application that our ROE should increase to reflect the Company's risk profile, and current economic and capital market conditions. Concentric indicated that our proposed ROE of 9.95% was *quote* "reasonable if not conservative" *unquote*.
- The Commission engaged its own expert, London Economics, who recommended that our ROE increase to 9.70%.
- Therefore, all the expert evidence on record confirms that our current ROE of 9.35% is too low.

However, during the negotiation, the PEI Energy Corporation wanted the ROE to remain unchanged at 9.35%.

- So, the compromise reached was an agreement to leave the ROE used to set customer rates unchanged at 9.35% and to allow an ROE of 9.70% to be used in the calculation of the Company's annual earnings.

- We believe that this compromise on ROE is **reasonable**, it **balances the interests of all stakeholders** and is **supported by the negotiated settlement as a complete package**, which includes the continuation of all regulatory deferrals.

### Deadband

This concept of an allowed ROE with a deadband to a higher ROE is extensively used by regulated electric and gas utilities. In fact, in our application (Exhibit M-1) on Table 5-21 on page 71, we presented other Canadian utilities that have an allowed ROE with a deadband. So this is a well-accepted practice.

To elaborate on this concept:

- customer rates will only reflect an ROE of 9.35%.
- In order for us to achieve an ROE of 9.70% in annual earnings, we will have manage the business by finding **cost efficiencies** and/or growing the business by **supporting electrification** and the **addition of new customers**.

The result of this negotiated ROE is a **\$3.6M decrease in the revenue** to be collected from customers over the 3-year period, as broken down in Table 2.

### **Energy Supply Cost – Table 3**

Table 3 reflects the revised debt repayment schedule that results in a **\$1.6M decrease** in energy supply costs, as broken down over the 3-year period.

- Subsequent to filing the GRA, the PEI Energy Corporation provided us with a revised debt repayment schedule related to their financing of the Point Lepreau debt, which lowered the revenue requirement by approximately \$1.6M.

Therefore, the energy supply cost, which rolls up into revenue requirement, was updated to reflect the revised repayment schedule.

So, these two items (the lower ROE and the revised debt repayment schedule), accounts for almost 90% of the total decrease in revenue requirement.

### **Two-Month Shift**

The remaining changes that I will discuss are due to:

- The impact of the first two changes, along with
- The shift in the effective date of new rates from March 1 to May 1.

With respect to the shifting of the effective date:

- The Commission approved the negotiation in mid-January, and as the negotiation progressed into February, we knew that it was not possible for this regulatory process to conclude in such time as to allow new rates to be effective March 1. Therefore, we needed to select an alternate date, but we wanted that date to be as soon as possible and still be achievable - and choose May 1.

### **ECAM Deferral**

Turning to Table 4,

- the change in effective date to May 1 results in a change in how this \$757K (approx. \$760K) is collected from customers
- In this settlement, it's part of the revenue requirement and collected in basis rates, while in the original application, this amount was collected through the ECAM rate adjustment
- So, this is just a shift in how the amount is collected.

The operation of the ECAM deferral requires two rates: (i) the ECAM base rate; and (ii) the ECAM rate adjustment.

The first rate, the ECAM base rate, determines the annual energy supply cost. The ECAM base rate is multiplied by the amount of energy produced and purchased, and that calculated amount is recognized on the Company's income statement as net energy supply cost and it's collected from customers as part of basis rates.

The second rate, the ECAM rate adjustment, essentially collects the amount deferred to the ECAM account. So, when actual energy supply costs exceed what is collected by the ECAM base rate, that difference is deferred to the ECAM account. Likewise, when actual energy supply costs are lower than what is collected, that difference is also deferred to the ECAM account. Then, that net ECAM balance is collected from customers through the ECAM Rate Adjustment.

Table 5 addresses the ECAM base rate and Table 10, which I'll get to a little bit later, addresses the ECAM Rate Adjustment.

#### ECAM Base Rate

Line G shows the revised ECAM base rate for each of the 3 years, and each year is slightly different from the rate proposed in the GRA.

And this is **caused by the two month shift** in the effective date of new rates. And I will try to explain why:

- Back in 2021, the Commission issued an order on our comprehensive review of the ECAM account.
- That order requires a select number of energy supply cost accounts to be excluded from the ECAM deferral
- And that exclusion is to be incorporated in this GRA.

So, the two-month shift in the effective date result in those select accounts continuing to be included in the ECAM deferral for an additional two months.

- Thereby increasing the energy supply costs attributable to ECAM by \$630K (line B). The detailed calculation of this \$630K was provided in our response to Commission IR-55.
- And this change in 2023 has a domino effect of slightly changing the amounts for the next two years.

To reiterate, the combined impact of this change to the ECAM base rate, and the change to the ECAM rate adjustment (which I'll get to in a moment) – is shifting the collection of the \$760K from the rate rider to basis rates.

- So, we're collecting more through the ECAM base rate and less through the ECAM rate adjustment.

### **Amortization – Table 6**

Amortization of the Provincial debt repayment costs decreased by a total of \$278K, as broken down over the 3-year period, to reflect:

- The continuation of the current rate rider that collects the debt repayment costs from customers for two additional months, and
- the revised repayment schedule from the PEI Energy Corporation.

### **Finance Charges – Table 7**

Table 7 shows that finance charges increased slightly, for a total of \$25K, as broken down over the 3 years to simply reflect the **timing of cash flows**.

### **Income Tax – Table 8**

Table 8 shows that income tax expense decreased by \$1.6M, as broken down over the 3 years to simply reflect the tax effect of all of the other changes.

### **Other Revenue – Table 9**

Table 9 shows that other revenue decreased by \$452K, as broken down over the 3 years.

- Which was due to an additional two months of over collecting the 2020 Revenue Shortfall.

As a reminder:

- The Revenue Shortfall is a regulatory deferral that allowed the Company to collect a \$2.8M shortfall in the revenue requirement for 2020.
- This Revenue Shortfall was approved by the Commission back in December 2020 in the same order that approved new rates effective January 2021.
- Within those rates, the Revenue Shortfall was to be collected over a 14-months period. However, those rates carried on and in March 2022 the



Company started to over collect the Revenue Shortfall, and that over collection continued for 12 months to February 2023 and was deferred. Our GRA reflected this over collection being refunded to customers.

- The two-month shift in the effective date results in the over collection of the Revenue Shortfall for an additional two months (approx. \$400K).
- And that's what's causing this adjustment.

So this concludes my discussion of the \$5.8M decrease in revenue requirement, which is primarily due to:

- A lower ROE, and
- the revised debt repayment schedule.

Next I will talk about the changes to the **Rate Riders**.

### **Rate Riders**

I will talk about three rate riders:

1. ECAM Rate Adjustment,
2. The rider to refund the net balance of the RORA and Revenue Shortfall, and
3. Energy Efficiency and Conservation Plan rate rider

### ECAM Rate Adjustment – Table 10

As I previously mentioned, the ECAM Rate Adjustment is essentially how the ECAM deferral balance is collected from customers.

The change in the rate for each of the 3 years, as outlined in Table 10, is due to the shift in the effective date by two months.

- The ECAM deferral operates on a continuum and when something changes the balance in one point in time, such as the shift in the effective date, that has a domino effect on the calculations that come after that change.
- And that is what is causing the changes per Table 10.

To recap, these changes in the ECAM Rate Adjustment, along with the changes to the ECAM Base Rate which I've previously discussed, simply shifts the collection of approx. \$760K from the rate rider to revenue requirement.

### RORA and 2020 Revenue Shortfall Rider – Table 11

The next rate rider is the netting of the Rate of Return Adjustment, or RORA balance against the 2020 Revenue Shortfall, which I've already discussed.

So now, I'll explain the RORA balance (but the story is the same as what I already discussed for the Revenue Shortfall):

- The RORA, first approved in 2011, captures any collections from customers that exceeds the approved ROE.
- When the Commission approved new rates effective January 2021, included was a refund of the RORA balance over a 14-month period.

- When those rates carried on, beyond the 14-month period, the Company started to over refund the RORA balance.
- The over refund from March 2022 to February 2023 was reflected in the original application.
- The two-month shift in the effective date results in the over refund for of the RORA balance for an additional two months; changing the over refund from \$53K to \$223K.
- I would like to point out a labelling error in Table 11
  - RORA is an over refund, not an over collection, and
  - Revenue Shortfall is an over collection, not an over refund.

And this rider simply nets the RORA balance against the Revenue Shortfall balance and the net result is a slight increase in the refund rate, as shown by line E.

#### Energy Efficiency and Conservation Rider – Table 12

The final rider collects from our customers a set amount to fund the PEI Energy Corporation's demand side management program, which is known as their Energy Efficiency and Conservation Plan. These funds are ultimately remitted to the PEI Energy Corporation.

As indicated in the GRA, the PEI Energy Corporation was forecasting an over collection from Maritime Electric customers, and the shift in new rates to May results in an additional two months of that over collection.

- This reduces the amount that needs to be collected from our customers for the 12-month period beginning March 2024.

And that concludes my discussion on the rate riders.

### **Weather Normalization**

The final item I would like to discuss is the Weather Normalization Mechanism and Reserve Account, which I'll simply refer to as Weather Normalization.

My intention is to leave you with an overview of the Weather Normalization. And we have Bob Younker with us today who will be available to answer any of your more detailed questions on this deferral.

The first point I would like to make is that **the continued approval of all regulatory deferrals, including this one, is a critical element of the negotiated settlement.**

- In general, an ROE is meant to compensate the utility for the risk it assumes in providing service to customers as a result of being regulated and its obligation to serve.
- In this particular situation, the negotiated ROE was based on the continued approval of all our regulatory deferrals. And if one or more of those deferrals are not approved, then the foundation upon which the ROE is based starts to erode and the ROE itself will need to be adjusted.

We appreciate that the Commission has questions about the continued approval of this deferral; therefore,

- the negotiated settlement indicated that an interim approval of this deferral would be acceptable, and
- we proposed a comprehensive review of this deferral account be undertaken to allow the Commission to make a fully informed decision on the operation of this deferral beyond the current rate-setting period.

There are two elements of the Weather Normalization that I would like to discuss:

1. The fundamentals of how it operates and why that's important, and
2. Why it's a material deferral

### Fundamentals

To begin, I'd like to start with one of the fundamental principles of cost of service regulation and that's a utility should be provided a fair opportunity to recover its full cost of service.

- What this really means is that if there is a risk that the utility will not recover its full cost of service and that risk cannot be controlled by the utility, then that risk needs to be mitigated.

- For example, Maritime Electric cannot fully control its energy supply costs. There are a number of factors that cause energy supply costs to materially exceed our forecast and we have no ability to bring those costs back down. Therefore, we have the ECAM deferral, which mitigates this risk. In the absence of the ECAM, our energy supply costs could increase to a level where our annual earnings would be materially reduced.

Our view is that the Weather Normalization deferral serves the same purpose as the ECAM deferral.

- To begin, I'm sure we can all agree that Maritime Electric cannot control the weather.
- Next, I want to explain how weather can materially impact our revenue. And that requires going back to how rates are set.
- Once our revenue requirement is determined and approved, it is essentially divided by our forecast of energy sales to arrive at a "per kWh" rate.
  - Revenue divided by forecast sales = rate
- Now I want to talk about that forecast of energy sales. In trying to predict how much energy our customers will consume, we break that down into two main categories: (i) energy for heating their home and (ii) energy for everything else.

- The energy used for space heating depends on how cold we think it's going to be. The best information we have for predicting future weather is historical weather. So we look back and measure how cold it's been over the past 10 years. And we use Heating Degree Days as that measurement. So we take the 10-year average of HDD and use that in our calculation of future energy consumption for space-heating purposes.
- Another key fact that we can agree on, is that here on PEI, when the weather is colder we turn up the heat and consume more energy.

*[can we refer to **Exhibit M-15, and IR-47**]*

And this brings me to how the Weather Normalization operates.

- So, as I just said, we use the 10-year historical average of HDD in our forecast of energy sales – which is the red line.
- And the blue line is actual HDD.
- The Weather Normalization compares actual HDD (blue line) to forecast (red line which is based on the 10-year historical average).
  - So if actual HDD are higher than forecast (as it was in 2019), it means the weather was colder than the 10-year average and we sold more energy than forecast.
  - If we sold more energy than forecast, it means we over collected the approved revenue requirement.
- And the Weather Normalization would capture that over collection to be refunded to customers. That is how the Weather Normalization serves to benefit the customer.

*[turn to the next page]*

- Chart 2 shows the actual Weather Normalization balance.
- If we look at 2019 on this chart, this shows the Weather Normalization was a balance owing to customers.
- So, when weather is colder than forecast, we over collect the revenue requirement, and the Weather Normalization captures that over collection to be returned to customers.
- The same thing happens when weather is warmer than normal

*[turn back to the previous page]*

- Let's look at 2021.
- Here, the weather was warmer than normal, meaning customers didn't need to turn up their heat like we thought they would,
- which means we sold less energy than forecast and under collected the approved revenue requirement.
- This under collection due to weather being different than the 10-year historical average is something Maritime Electric cannot control.
- Therefore, the Weather Normalization is a critical deferral that mitigates this risk.
- And at the same time, it serves to protect the customer if the weather impact swings the other way.
  - Which we can clearly see for this 10-year period

Before I go further, I'll pause to take any questions on what I've just explained.



So, to recap:

- If actual HDD turned out to be the same as the 10-year average (meaning the blue line would be the same as the red line)
  - This would mean that we collected the forecast revenue requirement related to space-heating load.
- Because the blue line is different from the red line, it means that some time we collect too much (when the blue line is above) and sometimes we don't collect enough (when the blue line is below).
- Which demonstrates the critical function of the Weather Normalization deferral. It serves to protect both the customer and the utility from uncontrollable weather impacts on the collection of revenue.

### Materiality

The next topic is why the Weather Normalization is a material deferral.

With respect to materiality, London Economics felt that the Weather Normalization was not a material deferral for Maritime Electric. And in Exhibit M-13, which is our response to London Economics' report, we tried to explain why we disagree with that conclusion.

*[turn to Chart 2 in Exhibit M-15, IR-47]*

When London Economics reviewed our Weather Normalization, they used the balance up to December 2020 (which was a \$1.2M balance recoverable from customers, before the balance flips in the other direction).

- London Economics looked at the left section of the chart, which is when weather was warmer than normal and we did collect enough revenue from customers, and the largest amount of \$470K, which is no material.
  - And I agree with that
- However, London Economics did not have this information, where the under collection grew to \$1.8M at the end of 2021. They didn't have this information when they concluded that the Weather Normalization was not material.
  - And that's what I disagree with.
  - \$1.8M is material to Maritime Electric.

I hope this helps you understand why the Weather Normalization is material to Maritime Electric. It's continued approval is an critical component of this negotiated settlement as a complete package that provides a reasonable and balanced outcome for all stakeholders.

*[can we go back to Exhibit M-14 and page 8]*

### **Impact on Customer Rates**

Table 13 simply highlights the change to the residential customer rate as per the settlement in comparison to the GRA.

- So the \$5.8M reduction in the revenue requirement reduces the residential rate from 3% per year to 2.6% in years 1 and 2 and 2.7% in year 3.

## Rate Design Application

This last section was meant to acknowledge the pending Rate Design proceeding and that the outcome of the Rate Design Application can be layered upon the outcome of the GRA.

## Conclusion

*[go back to Table 1 at the beginning of this exhibit]*

To conclude my discussion of the negotiated settlement:

- The revenue requirement is reduced by \$5.8M which is primarily due to the lower ROE and revised debt repayment schedule.
- These two changes in combination with a two month shift in the effective date for new rates results in other minor changes to the revenue requirement and a change is various rate riders.
- The settlement proposes that the Weather Normalization continue to approved on an interim basis, rather than on a permanent basis, and that the Company recommends a comprehensive review of this deferral to allow the Commission to make a fully informed decision on its approval before the next GRA is filed.

We believe that this settlement, as a complete package, is **reasonable** and **balances the interests of all stakeholders**. Thank you.

And I'd be happy to answer any additional questions you have.