February 26, 2010

By RESS and Courier

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
M4P 1E4

Re: Electricity Distribution Licence ED-2006-0031
Distribution Rate Application 3rd Generation Incentive Regulation Mechanism
EB-2009-0228

Dear Ms Walli,

Please find attached the final reply submission for Horizon Utilities Corporation in the above captioned proceeding.

Yours truly,

Original signed by Indy Butany-DeSouza

Indy J. Butany-DeSouza
Vice President, Regulatory and Government Affairs
Horizon Utilities Corporation

EB-2009-0228

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, (Schedule B);

AND IN THE MATTER OF an Application by Horizon Utilities Corporation to the Ontario Energy Board for an Order or Orders approving or fixing just and reasonable rates and other service charges for the distribution of electricity as of May 1, 2009.

HORIZON UTILITIES CORPORATION ("HORIZON UTILITIES")

REPLY ARGUMENT
DELIVERED FEBRUARY 26, 2010

Introduction:

1. Horizon Utilities Corporation ("Horizon Utilities") is a licensed electricity distribution company operating in the City of Hamilton and the City of St. Catharines under Ontario Energy Board (the "OEB" or the "Board") Electricity Distribution Licence ED-2006-0031.

2. On November 4, 2009, Horizon Utilities made an Application to the OEB for an order or orders pursuant to Section 78 of the *Ontario Energy Board Act, 1998*, as amended (the "OEB Act") for approval of its distribution rates and other charges, effective May 1, 2010 (the "Application". Based on the Application, a typical Residential customer (consuming 800 kWh/month) would experience a bill decrease of $0.25, or 0.3% per month. A small General Service < 50 kW customer (consuming 2,000 kWh/month) would experience a bill decrease of $0.67, or 0.3% per month.

3. Horizon Utilities has followed Chapter 3 of the OEB's *Filing Requirements for Transmission and Distribution Applications* issued July 22, 2009 (the "Chapter 3 Requirements"); and the Filing Instructions provided in the OEB's 2010 3rd

Generation Incentive Regulation Mechanism (IRM3) model ("Rate Generator Model"), the 2010 Incentive Regulation Mechanism Supplemental Filing Module ("Supplementary Filing Module"), and the 2010 Incentive Regulation Mechanism Deferral and Variance Account workform ("Deferral and Variance Account Model"), referred to collectively as the "Models", as provided to distributors by the OEB.

4. In its Application, Horizon Utilities did not propose to dispose of the balances in its "Group 1 Accounts", as those accounts are described in the Board's *Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report"), for the reasons set out in the Application.

5. Horizon Utilities published notice of its Application as required by the OEB. The notice set out the impacts described above. No parties expressed an interest in participating in this proceeding. Only Board staff participated in this proceeding. Horizon Utilities filed responses to Board staff interrogatories on January 13, 2010. Board staff filed its written submission on February 10, 2010.

6. Board staff's submission addressed three matters:

   (a) Disposition of Deferral and Variance Accounts as per the *Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report");

   (b) Adjustments to the Retail Transmission Service Rates; and

   (c) Accounting for the implementation of the Harmonized Sales Tax ("HST".)

7. Horizon Utilities offers replies to the Board staff submissions, as follows.

Disposition of Deferral and Variance Accounts as per the EDDVAR Report

8. Board staff took issue with Horizon Utilities' proposal that the $19.5 million credit balance in the Group 1 Deferral and Variance Accounts not be disposed of in 2010 on the basis that since the preset disposition threshold is exceeded, the expectation is that it will be disposed of in one year. In the alternative, Board staff submitted that the onus is on the distributor to justify why the account balance in excess of the threshold should not be cleared.

9. Board staff noted that Horizon Utilities, based on an extrapolation of the accounts, projected that by April 2011 the account credit would largely disappear. Horizon Utilities therefore considered a current disposition of the credit balance as redundant and not in the best interests of customers and Horizon Utilities, as it would have to be followed almost immediately by an application for recovery of a significant debit balance from customers[1].

10. Board staff noted that the projected growth (debit) in the global adjustment sub account largely accounted for the disappearance of the existing credit balance. Board staff wondered whether that balance would continue to grow at the same rate as it did over the December 31, 2008 to September 30, 2009 period.

Based on more current information, Horizon Utilities notes that the growth rate in the global adjustment sub-account is somewhat less than originally expected. While the balances in the Group 1 accounts are, as suggested in Horizon Utilities' initial application, declining, they are doing so at a different pace. As indicated in the table below, the total balances have declined from ($19,466,721) at December 31, 2008 to ($12,687,033) at September 30, 2009, a reduction of over one-third of the total balance in nine months. The balances at December 31, 2009 are ($17,149,067) another one-third swing from the balances at September 30, 2009.

[1] Manager's Summary, p. 9, para. 23-25

11. Horizon Utilities is very concerned with the volatility experienced by these accounts. If Horizon Utilities disposes of (refunds) the balances as at December 31, 2008 and the accounts continue the declining trend, Horizon Utilities would shortly thereafter be proposing a charge to its customers to recover the balances. Rate adjustments that provide for decreases one year followed by increases the next are not practical for many reasons. From a customer perspective, budgeting is impossible with such changes in rates. Rate stability is an important component of rate design, which begs the question why dispose of the accounts at this time. When the accounts are closer to zero, as Horizon Utilities had anticipated they may be by April 30, 2011, Horizon Utilities would have avoided both a rate decrease (to cover the balances at December 31, 2008), and a subsequent rate increase (to cover the changes from December 31, 2008 to April 30, 2011). From a corporate perspective, as stated in the initial Application, Horizon Utilities would be required to unnecessarily incur significant additional debt and related interest charges if it were to refund the balances at December 31, 2008[2]. Any disposal of accounts will cause a negative impact on Horizon Utilities' cash flow position at a time when Horizon Utilities (and other utilities) are feeling the effects of a downturn in the economy. Horizon Utilities submits that the present trend of disposition of the Group 1 Accounts based on existing rates is sufficient to meet the objectives of the EDDVAR Report. Horizon Utilities notes that the Board has discretion to depart from the EDDVAR Report when it is in the public interest to do so.[3] Horizon Utilities also notes that the Board has recognized the cash flow challenges facing distributors (for example, in the case of Enersource Hydro Mississauga Inc., due to significant increases in the Global Adjustment sub-account balance).[4] Finally, Horizon Utilities notes that the Board has recently observed that with declines in electricity demand (and therefore in spot market prices) coupled with increases in supply, much of it at fixed price

[2] Manager's Summary, p. 7, para. 24 a)
[3] See the Board's January 29, 2010 Decision in Enersource Hydro Mississauga's application to dispose of certain deferral and variance account balances (EB-2009-0405), at p.5.
[4] *Ibid,*, at p.3

contracts entered into with the Ontario Power Authority (the "OPA") under which the OPA pays the difference between the spot and contract prices, the Board does not anticipate balances in the global adjustment sub-account to reverse themselves any time soon.[5]

12. Accordingly, Horizon Utilities reiterates its request, as set out in the Application, that the Board not require it to dispose of its Group 1 Deferral and Variance Account balances at this time.

13. In the alternative, should the Board conclude that Horizon Utilities should dispose of some portion of the Group 1 accounts, Horizon Utilities refers to the January 29, 2010 Decision and Order of the Board in the matter of an Application by Enersource Hydro Mississauga Inc. ("Enersource") for an order or orders to dispose of certain deferral and variance account balances (EB-2009-0405). In that Decision, the Board granted Enersource's request to dispose of its Group 1 account balances as of December 31, 2008 (other than account #1588 - GA). The Panel also approved Enersource's proposal to dispose of the balance in account #1588 – GA as of September 30, 2009. For Horizon Utilities, using these dates and balances, the total to be disposed of is $12,369,859 as shown in the table below. The material increase in the global adjustment sub-account balance during 2009 has had a negative effect on Horizon's cash flow position. For this reason, using the September 30, 2009 balance in the #1588 – Global Adjustment account is reasonable and appropriate.

[5] *Ibid.*, at p.7

ALTERNATIVE DATES			
Horizon Utilities Corporation Regulatory Assets / (Liabilities) Analysis			
	G/L Account #	Date of Balance	Balance
RSVA - WMS	1580	Dec/08 Balance	(11,230,990.61)
RSVA -NW	1584	Dec/08 Balance	(6,611,358.29)
RSVA - CN	1586	Dec/08 Balance	384,110.19
RSVA - Power	1588	Dec/08 Balance	(2,407,307.41)
RSVA - Power Adj	1588	Sept/09 Balance	8,265,380.00
Low Voltage	1550	Dec/08 Balance	(769,692.81)
			(12,369,858.93)

14. If the Board were to select this alternative approach, Horizon Utilities proposes that the balance of $12, 369,858 be disposed of over two years consistent with the Board's treatment of the recovery in the Enersource Decision. Further, the two year period is consistent with the period over which the balances accrued.

Adjustments to the Retail Transmission Service Rates ("RTSR")

15. Board staff noted that Horizon Utilities has applied for an adjustment to its RTSR rates based on a comparison of Retail Transmission Service revenue under existing rates and adjusted wholesale transmission costs and that Horizon Utilities is requesting an increase of 7.942% for its Network Service Rate and a decrease of 4.760% for its Line and Transformation Connection Service Rate. In Board staff's view, Horizon Utilities has provided a reasonable analysis and explanation as part of its original application.

16. Board staff noted that while Horizon Utilities did include in its 2009 rates the July 1, 2009 level of Uniform Transmission Rates ("UTRs"), it may wish to update its rates for 2010 pursuant to Board's Decision and Rate Order, EB-2008-0272, as follows:

- The Network Service Rate has increased from $2.66 to $2.97 per kW per month, an 11.7% increase over the July 1, 2009 level or 15.6% over the rate in effect prior to July 1, 2009;
- The Line Connection Service Rate has increased from $0.70 to $0.73 per kW per month; and
- The Transformation Connection Service Rate has increased from $1.57 to $1.71 per kW per month, for a combined Line and Transformation Connection Service Rates increase of 7.5% over the July 1, 2009 level or 5.2% over the rate in effect prior to July 1, 2009, since distribution rates would have been implemented on May 1, 2009.

17. Horizon Utilities has considered the Board staff comments, and has recalculated its Retail Transmission Service Rates in accordance with the Rate Order issued January 21, 2010 revising the UTRs effective January 1, 2010, in keeping with the Board staff suggestion.

18. Revised Table 1 below provides Horizon Utilities' calculations of the IESO transmission network and connection charges for twelve months at existing rates and the approved new rates.

			Revised Table 1						
			IESO CHARGE FOR TRANSMISSION						
* **Based on Existing rates**									
Forecast for Rate Year	**NW Total $**	**Rate**	**kW**	**Trans CN Total $**	**Rate**	**kW**	**Line CN Total $**	**Rate**	**kW**
May-10	1,646,354	2.66	618,930	1,042,142	1.57	663,785	431,201	0.70	616,001
Jun-10	2,184,421	2.66	821,211	1,355,604	1.57	863,442	557,647	0.70	796,638
Jul-10	2,010,723	2.66	755,911	1,258,176	1.57	801,386	519,447	0.70	742,067
Aug-10	2,510,606	2.66	943,837	1,566,328	1.57	997,661	649,380	0.70	927,686
Sep-10	2,533,727	2.66	952,529	1,538,774	1.57	980,111	639,911	0.70	914,159
Oct-10	1,965,671	2.66	738,974	1,258,835	1.57	801,806	517,465	0.70	739,236
Nov-10	2,039,374	2.66	766,682	1,283,141	1.57	817,287	534,593	0.70	763,704
Dec-10	2,112,769	2.66	794,274	1,330,410	1.57	847,395	553,513	0.70	790,733
Jan-11	2,063,043	2.66	775,580	1,285,425	1.57	818,742	533,027	0.70	761,467
Feb-11	2,039,031	2.66	766,553	1,271,256	1.57	809,717	523,677	0.70	748,110
Mar-11	1,991,494	2.66	748,682	1,265,712	1.57	806,186	521,219	0.70	744,598
Apr-11	1,729,431	2.66	650,162	1,114,240	1.57	709,707	455,405	0.70	650,578
Total for May10-Apr11	**24,826,645**			**15,570,043**			**6,436,484**		
Total Network	**24,826,645**						Total Connection		**$ 22,006,527**
* **Based on Revised rates**									
Forecast for Rate Year	**NW Total $**	**Rate**	**kW**	**Trans CN Total $**	**Rate**	**kW**	**Line CN Total $**	**Rate**	**kW**
May-10	1,838,222	2.97	618,930	1,135,072	1.71	663,785	449,681	0.73	616,001
Jun-10	2,438,997	2.97	821,211	1,476,486	1.71	863,442	581,546	0.73	796,638
Jul-10	2,245,056	2.97	755,911	1,370,370	1.71	801,386	541,709	0.73	742,067
Aug-10	2,803,196	2.97	943,837	1,706,000	1.71	997,661	677,211	0.73	927,686
Sep-10	2,829,011	2.97	952,529	1,675,990	1.71	980,111	667,336	0.73	914,159
Oct-10	2,194,753	2.97	738,974	1,371,088	1.71	801,806	539,642	0.73	739,236
Nov-10	2,277,046	2.97	766,682	1,397,561	1.71	817,287	557,504	0.73	763,704
Dec-10	2,358,994	2.97	794,274	1,449,045	1.71	847,395	577,235	0.73	790,733
Jan-11	2,574,926	3.32	775,580	1,522,860	1.86	818,742	555,871	0.73	761,467
Feb-11	2,544,956	3.32	766,553	1,506,074	1.86	809,717	546,120	0.73	748,110
Mar-11	2,485,624	3.32	748,682	1,499,506	1.86	806,186	543,557	0.73	744,598
Apr-11	2,158,538	3.32	650,162	1,320,055	1.86	709,707	474,922	0.73	650,578
Total for May10-Apr11	**28,749,317**			**17,430,108**			**6,712,333**		
Total Network	**28,749,317**						Total Connection		**$ 24,142,441**

Revised Table 2 below provides Horizon Utilities' calculations for transmission network and connection charges for wholesale delivery points embedded in the Hydro One Networks Inc. distribution systems. The Hydro One transmission network and connection charges used are at existing transmission rates and the approved new transmission rates.

Revised Table 2 Hydro One Embedded Points				
Based on Existing Rates				
Month	**Connection Charge Quantities**	**Network Charge Quantities**	**Connection Charges ($)**	**Network Charges ($)**
May-10	55,438	53,214	110,322	119,199
Jun-10	77,021	75,678	153,272	169,519
Jul-10	72,072	70,370	143,423	157,629
Aug-10	85,122	84,154	169,393	188,505
Sep-10	76,833	70,701	152,898	158,370
Oct-10	58,619	57,194	116,652	128,115
Nov-10	84,537	82,544	168,229	184,899
Dec-10	64,483	64,305	128,321	144,043
Jan-11	64,521	64,135	128,397	143,662
Feb-11	62,542	62,098	124,459	139,100
Mar-11	58,536	57,305	116,487	128,363
Apr-11	56,390	55,305	112,216	123,883
Total May09-Apr10	**816,114**	**797,003**	**1,624,067**	**1,785,287**
Based on Revised Rates				
Month	**Connection Charge Quantities**	**Network Charge Quantities**	**Connection Charges ($)**	**Network Charges ($)**
May-10	55,438	53,214	108,104	123,456
Jun-10	77,021	75,678	150,191	175,573
Jul-10	72,072	70,370	140,540	163,258
Aug-10	85,122	84,154	165,988	195,237
Sep-10	76,833	70,701	149,824	164,026
Oct-10	58,619	57,194	114,307	132,690
Nov-10	84,537	82,544	164,847	191,502
Dec-10	64,483	64,305	125,742	149,188
Jan-11	64,521	64,135	136,785	166,110
Feb-11	62,542	62,098	132,589	160,834
Mar-11	58,536	57,305	124,096	148,420
Apr-11	56,390	55,305	119,547	143,240
Total May10-Apr11	816,114	797,003	**1,632,561**	**1,913,535**

Table 4 below provides a summary of the total wholesale transmission costs as compared to the retail transmission billing amounts based on proposed rates. As can be seen, the amounts paid equal the amounts billed. This analysis confirms that the new proposed retail transmission rates have been set at the levels required so that additional RSVA transmission network and RSVA transmission connection variances should not accumulate in these accounts.

Revised Table 4					
Summary of IESO & Hydro One charges vs. Horizon Utilities Billed all at New Rates					
	A	**B**	**C = A + B**	**D**	**C-D**
Description	**IESO Charged**	**Embedded Points**	**Total**	**Horizon Billed**	**RSVA Balance**
Connection	24,142,441	1,632,561	25,775,001	25,775,001	0
Network	28,749,317	1,913,535	30,662,852	30,662,852	(0)

Accounting for the implementation of the Harmonized Sales Tax ("HST")

19. Board staff have suggested that, with the implementation of the Harmonized Sales Tax ("HST") on July 1, 2010, utilities will start to realize cost savings. The costs savings would result from the replacement of the provincial 8% sales tax with a harmonized consumption tax, the underlying assumption being that the costs recovered through existing rates include a provincial tax component for those goods and services currently subject to the existing provincial sales tax. Board staff refer to provincial and federal government pronouncements to illustrate the significant savings the HST will generate as a reason to warrant the establishment of a deferral account, effective July 1, 2010, to record any such savings. Board staff also questioned Horizon Utilities' view that the tracking of actual savings will be administratively burdensome, in light of federal and provincial governments' expectations regarding the stimulative and competitive benefits that will ensue from harmonization.

20. Horizon Utilities questions the regulatory basis for Board staff's proposal that any cost savings from harmonization should be recorded in a deferral account for future disposition. Horizon Utilities submits that this approach is not appropriate at this time, for the reasons set out below.

21. In the 3GIRM model, tax changes to the Ontario Capital Tax Rates and changes in the Corporate Tax Rates are built into the model. The relative simplicity in applying the changed tax rates allows the impacts to be incorporated into the model. HST is not an income tax but is a sales, or value added tax ("VAT") and as such, does not warrant the same treatment as the current tax changes incorporated as part of the 3GIRM. The difficulty and uncertainty in determining the exact nature and quantity of the impact of the change in the sales tax necessitates that it not be considered as an income or corporate tax.

22. To begin, there is no way to determine accurately and efficiently the amount of the HST 'savings'. The savings are identified as the difference between what is paid as the equivalent PST under the new HST rules, and PST paid prior to the implementation of HST. In order to determine the exact amount of the savings, there would have to be a comparison between an invoice received and paid prior to the implementation of HST and one received and paid after. To determine the correct difference, that which should be recorded in the variance account, all details of the purchases would have to be the same, including (among other factors) the item purchased, the quantity purchased, and delivery options. If the conditions were exactly the same then PST paid in the former regime could be compared to the PST portion of HST, and the difference recorded in the variance account. In other words, recording the portion of the HST that relates to the former PST is one half of the savings equation. Without the other half of the equation, the portion of PST actually paid prior to HST, the correct difference can never be accurately determined. Furthermore, PST was never recorded as a separate component of OM&A or capital costs in the 2008 EDR Application, making a fair comparison between what was paid in the past compared to what is

currently paid, impossible to determine. If the subsequent price of the item changed, there would still be the uncertainty as to why the price changed. Horizon Utilities would have no way of determining how much of the change is due to the HST and how much is the result of the vendor's market factors.

23. Until HST comes into effect, and is in effect for a number of years, the impact on the pricing structure of goods and services purchased by Horizon Utilities, or any other business, cannot be known. Some goods and services had no PST applied to them when purchased or sold, but will have the full impacts of HST applied under the new HST mechanism. Horizon Utilities anticipates that vendors will take advantage of the opportunity to adjust their prices, with the government as an easy target for "blame". Prices will no doubt be adjusted, but the change due specifically to the HST will be extremely difficult, if not impossible, to determine. The phased implementation of HST is a clear indication that the government is expecting a period of adjustment to the implementation of HST. As an example, electricity sales did not previously have PST applied but will do so after July 1, 2010. The Input Tax Credit ("ITC") is restricted so that only a portion is claimable. Once again, this makes the accurate determination of any savings more challenging.

24. Moreover, even if the difference could be accurately determined, that is only one portion of the calculation. Horizon Utilities anticipates that the administrative burden to compare each current invoice to an invoice received prior to the implementation and to train payables clerks in PST matters, could eliminate a large portion, if not all of the savings, if in fact there are savings. These costs must be reflected in any variance account.

25. In addition, there will be an impact on the timing of cash flows for Horizon Utilities and all distributors, since HST will be applied to purchases of electricity from the IESO. The associated ITC can only be claimed at a later date. This creates an

adverse effect on working capital which would have to be quantified and applied against any savings in the deferral account.

26. Finally, sales of electricity to Horizon Utilities' customers will include the full effects of the HST, effectively a cost increase of 8%. Horizon Utilities expects that bad debt expenses could increase by at least 8% as a result of the HST implementation. As with the impacts on working capital discussed above, any increased bad debt costs should be considered when attempting to determine the savings, if any, resulting from HST implementation.

27. If the Board does decide to implement a deferral account, Horizon Utilities submits that it should only be the difference in net costs between the PST environment prior to July 1, 2010, and the HST environment after July 1, 2010 that should be recorded in that account, and the calculation of that difference must include the additional costs discussed above

28. Horizon Utilities submits that the implementation of HST, because it affects all distributors, should be the subject of a generic Board proceeding, and should not be determined in the course of individual distributors' rate applications.

29. Finally, Horizon Utilities notes that Board staff are not proposing any other changes in the 2010 IRM process, such as changes reflecting the methodology set out in the Board's December 11, 2009 Report on the Cost of Capital for Ontario's Regulated Utilities. Horizon Utilities submits that the appropriate and equitable time to address the impacts of the change to an HST regime is at the time of its next rebasing, and not during the IRM process.

Conclusion

30. For all of the foregoing reasons, Horizon Utilities requests that the Board:

(a) Confirm that Horizon Utilities' Group 1 Deferral and Variance Account balances will not be disposed of as part of Horizon Utilities' schedule of rates and charges that will come into force May 1, 2010;

(b) Approve Horizon Utilities' recalculated Retail Transmission Service Rates based on the OEB Rate Order issued January 21, 2010 which revised the Uniform Transmission Rates effective January 1, 2010; and,

(c) Confirm that no adjustments or variance accounts will be required at this time with respect to the upcoming change to an HST regime.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 26TH DAY OF FEBRUARY, 2010:

HORIZON UTILITIES CORPORATION
Per:

Original signed by Indy J. Butany-DeSouza

Indy J. Butany-DeSouza
Vice President, Regulatory & Government Affairs

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