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Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2009 ELECTRICITY DISTRIBUTION RATES

Lakefront Utilities Inc.

EB-2008-0193

January 29, 2009

INTRODUCTION

Lakefront Utilities Inc. ("Lakefront") submitted an application on November 7, 2008, seeking approval for changes to the rates that Lakefront charges for electricity distribution, to be effective May 1, 2009. The application is based on the 2009 Incentive Regulation Mechanism.

The purpose of this document is to provide the Ontario Energy Board (the "Board") with the submissions of Board staff after its review of all the evidence submitted by Lakefront.

2009 3rd GENERATION IRM SUPPLEMENTARY FILING MODULE

Background

For the purpose of calculating the revenue-to-cost ratio adjustments, the 2009 3rd Gen. IRM Supplementary Filing Module (the "IRM Module") allocates the low voltage charges and transformer allowance "costs" across rate classes in a way that differ from how they were allocated in Lakefront's 2008 cost of service application ("2008 CoS").

Discussion and Submission

As a result of the difference in methodology employed in the IRM Module as compared to the methodology used in the 2008 CoS, there may be a slight difference in the calculated revenue-to-cost ratios (the "Ratios") and the proposed adjustments that would result under each method. Board staff submits that this difference is immaterial and that Lakefront's proposed revenue-to-cost ratio adjustments are reasonable and in compliance with its 2008 cost of service Decision (EB-2007-0761).

Board staff notes that the *Report of the Board on the Application of Cost Allocation for Electricity Distributors* dated November 28, 2007 (the "Report") indicated that a range approach for Ratios was preferable given influencing factors, such as data quality. Accordingly, Board staff submits that the differences in the Ratios calculated in the IRM Module and under the 2008 CoS methodology would need to be material for a revision to the proposed revenue-to-cost ratio adjustments to be warranted at this time. As stated earlier, Board staff submits that those differences are immaterial.

Board staff would like to inform interested parties that the IRM Module will be adjusted next year to enable distributors to reflect how the low voltage charges and transformer allowance “costs” were allocated for the purpose of calculating their Ratios in their 2008 CoS. Accordingly, any differences in the calculation of the Ratios in the 2009 IRM Module will be reverted in the 2010 IRM Module next year.

REVENUE TO COST RATIO ADJUSTMENTS

Background

In Lakefront’s 2008 IRM Decision (EB-2007-0761), the Board directed that increased revenues be collected from the street lighting and sentinel lights. The Board further directed, at page 21 of the Decision, that “to the extent additional revenue is forecasted to be collected from the Street Lights and Sentinel Lights classes, the rates for the GS<50 kW and GS 50-2,999 kW classes shall be adjusted downward”.

Lakefront’s 2009 application (Sheet C3.1 of the 3rd Gen. IRM Supplementary Filing Module[1]) currently indicates:

- an increase in the Ratio for the Street Lighting rate class from 25.5% to 39.9%;
- an increase in the Ratio for the Sentinel Lighting rate class from 55.1% to 70.1%;
- a decrease in the Ratio for the GS 50 to 2,999 kW rate class from 169.4% to 164.3%;
- the Ratio for the GS<50 kW rate class will remain constant at 118.4%.

Discussion and Submission

Lakefront’s 2009 IRM application proposes to decrease the Ratio for the GS 50 to 2,999 kW rate class, while keeping the Ratio for the GS<50 kW rate class the same.

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[1] Note that the revenue-to-cost ratios calculated in the 2009 3rd Gen. IRM Supplementary Filing Module may differ from the ratios calculated in the 2008 cost of service application due to differences in the treatment of low voltage charges and the transformer allowance.

Board staff submits that this result is not consistent with the Board's specific directions in EB-2007-0761 that the additional revenues to be collected from the Street Lighting and Sentinel Lighting rate classes be applied to lower rates for both the GS<50 kW and GS 50 to 2,999 kW rate classes.

In its January 19, 2009 reply to Board staff interrogatory number 2, Lakefront provides the following rationale for its position:

> "By increasing the revenue-to-cost ratio for Street Lighting and Sentinel Lighting classes, LUI chose to apply the corresponding decrease to the GS>50-2,999KW class in recognition that this class is much further from the unity (100%) than all the other classes as demonstrated in the table below per sheet C3.1. (…)
>
> LUI believe the Board's decision and goal is to over time, move all customer classes to the unity, mitigating rate shock and maintaining reasonable rates within a distributor's territory. With the GS 50 – 2,999 kW class being the furthest from unity, LUI believes the reduction to this class is consistent with the Board's decision. The GS > 50-2,999 kW is 64.3% over unity whereas the GS < 50 Kw is 18.4% over unity."

Board staff submits the above argument does not take into account that the target range set out in the Report for the Ratio of the GS 50 to 2999 kW rate class (80 to 180%) is significantly larger than that for the GS<50 kW rate class (80 to 120%), and that the Board made a specific direction in Lakefront's 2008 Decision as to how future cost allocation adjustments were to be implemented. Moreover, Board staff observes that if both the Ratio of the GS 50 to 2,999 kW rate class and the Ratio of the GS<50 kW rate class are decreased, both of these Ratios will move closer to unity.

Board staff invites parties to comment on whether the increased revenue to be obtained from the Street Lighting and Sentinel Lighting rate classes should be used to decrease the Ratios of both the GS 50 to 2,999 kW and the GS<50 kW rate classes.

PAYMENT IN LIEU OF TAXES (PILs)

Background

On December 13, 2007, the Ontario government introduced its 2007 Ontario Economic Outlook and Fiscal Review. Bill 44, the enabling legislation, received Royal Assent on May 14, 2008, and was promulgated in The Ontario Gazette on May 24, 2008. The resulting tax changes affecting the electricity distributors are listed below:

<u>Effective January 1, 2007</u>

Small Business Credit
- Threshold increased from $400,000 to $500,000
- Claw-back rate decreased from 4.67% to 4.25%

Ontario Capital Tax
- Reduced from 0.285% to 0.225%
- Deduction increased from $10,000,000 to $12,500,000

<u>Effective January 1, 2008</u>

Ontario Capital Tax
- Deduction increased from $12,500,000 to $15,000,000

The Board's Decision in Lakefront's 2008 CoS application (EB-2007-0761) was issued on May 9, 2008, prior to Bill 44 becoming enacted. Accordingly, Lakefront's revenue requirement was calculated on the tax rates that existed prior to the enactment of Bill 44.

Discussion and Submission

Board staff notes that some 2008 CoS proceedings required more time to process than others. As a result, some applications that were filed with the Board at around the same time as Lakefront filed its 2008 CoS application had their Decisions issued after May 24, 2008, with their resulting electricity distribution rates reflecting the lower tax rates. Board staff submits that for consistency and fairness across electricity distributors, the difference in PILs Lakefront is collecting in its distribution rates as a result of its 2008 CoS Decision having been issued before May 24, 2008, should be removed as of May 1, 2009. Board staff also submits that the additional amounts Lakefront collected in the 2008 rate year should remain with Lakefront, as it appropriately reflected the Board Decision (EB-2007-0761) for that rate year.

In Board staff's submission, Lakefront's distribution rates should be adjusted to reduce the revenues collected by $28,554. This amount corresponds to the difference between $319,484 (the PILs calculated on page 13 of Lakefront's 2008 CoS rate order submission dated June 27, 2008) and $290,930 (the PILs calculated in cell E137 of Sheet F1.1 of the IRM Module). This difference is the result of changes to the small business credit provisions only; the changes to the Ontario capital tax did not affect Lakefront's total PILs. For ease of reference, the table below details the calculation performed in the IRM Module.

Lakefront's Grossed-up 2008 PILs Following the Enactment of Bill 44

Item	**Description**	**Reference**	**Rates $**	**PILs**
(1)	2008 CoS Taxable Income	EB-2007-0761	$717,129	
Ontario Taxes				
(2)	Income tax payable	(1) * 14%	$100,398	
(3)	Small business credit	-$500,000 * 8.5%	-$42,500	
(4)	Surtax	[(1) - $500,000] * 4.25%	$9,228	
(5)	Ontario Income tax		$67,126	
Combined 2008 Tax Rate and PILs				
(6)	Effective Ontario Tax Rate	(5)/(1)	9.36%	
(7)	Federal tax rate **in 2008**		19.50%	
(8)	Combined tax rate		28.86%	
(9)	PILs	(1) X (8)		$206,966
(10)	Grossed-up PILs	(9) / (1 - (8))		$290,930

Board staff asks the applicant to respond to staff's proposed adjustment of $28,554 to its distribution rates. Board staff also invites the applicant to contact Board staff for assistance in reflecting this proposed change in Lakefront's Excel models, if it agrees to the proposed adjustment.

Board staff's proposed adjustment of $28,554 is in addition to the tax sharing required from the reduction in the federal tax rate from 19.5% to 19% effective January 1, 2009.

This tax savings will amount to $7,036, with half to be returned to customers through a rate rider.

All of which is respectfully submitted.