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VIA MAIL and E-MAIL

May 4, 2009

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St.
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: EB-2008-0205
Oshawa PUC Networks Inc. – 2009 Electricity Distribution Rate Application
Submissions of the Vulnerable Energy Consumers Coalition (VECC)

Please find enclosed the submissions of the Vulnerable Energy Consumers Coalition (VECC) on the Applicant's evidence in the above-noted proceeding with respect to the Requested Incremental Capital Adjustment.

Thank you.

Yours truly,

Michael Buonaguro
Counsel for VECC

Encl.

OSHAWA PUC NETWORKS

2009 DISTRIBUTION RATE APPLICATION

(INCREMENTAL CAPITAL ADJUSTMENT)

BOARD FILE NO. EB-2008-0205

FINAL SUBMISSIONS OF THE VULNERABLE ENERGY CONSUMERS' COALITION

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INTRODUCTION

1. On November 11, 2008 Oshawa PUC Networks Inc. (OPUCN) filed its 2009 Distribution Rate Application. The Application was based on the Board's 3rd Generation IRM Plan and included a request for an Incremental Capital Adjustment.

2. Set out below is the Final Argument of the Vulnerable Energy Consumers' Coalition ("VECC") with respect to OPUCN's Application. The Argument is organized into the following sections:
   1) 3GIRM Incremental Capital Adjustment – General Approach
   2) Filing Requirements for Incremental Capital Module
   3) Request to Recover Regulatory Costs

3GIRM INCREMENTAL CAPITAL ADJUSTMENT – GENERAL APPROACH

OPUCNs Position

3. In its Application OPUCN applied the incremental capital threshold calculations as specified in the *Supplemental Report of the Board on the 3rd Generation Incentive Regulation for Ontario's Electricity Distributor's*. Based on the preliminary IRM parameters available in October 2008 OPUCN's Incremental Capital Threshold was $6,567,275[1]. With a projected capital budget of $11,803,824, the "potentially" eligible capital spending was determined to be $5,236,549[2].

4. OPUCN then reduced this amount by $1,705,249 to exclude projects that were deemed to be included in its base capital spending primarily due to carry over from 2008. The resulting difference ($3,533,300) represented the cost of four projects which OPUCN claimed were non-discretionary and unusual in the terms of being outside its normal spending requirements proposed. This formed the basis for OPUCN's original

[1] OPUCN's Incremental Capital Application (the « Application », page 3
[2] Application, page 3

application and its request for a rate rider to recover the associated $453,220 incremental revenue requirement[3].

5. During the course of the proceeding OPUCN updated its Application to reflect:
    - The final GDP-IPI value for 2009 of 2.3%,
    - Revised capital spending requirement for the Concrete Pole Replacement project, one for projects included in its Incremental Capital Adjustment, and
    - A reduced carry over in capital spending from 2008 to 2009 of $1.5M.

    As a result of these changes the total capital spending for 2009 (adjusted for the 2008 carry over) was reduced to $9 M[4]; the threshold for incremental capital spending increased to $6.7 M[5] and the cost of four projects for which incremental funding was being requested was reduced to $2,221,500[6].

VECC's Submissions

Circumstances Qualifying for ICM

6. The Board's September 2009 Supplementary Report stated[7] that "the capital module is intended to be reserved for unusual circumstances that are not captured as a Z-factor and where the distributor has no other options for meeting its capital requirements within the context of is financial capabilities underpinned by existing rates".
7. In VECC's view the incremental capital adjustment is not applicable to all circumstances where a utility's capital spending program exceeds depreciation. Indeed the Board specifically considered and rejected such circumstances as qualifying for the Incremental Capital Module. This is can be clearly seen from following excerpt from the Board's September 2008 Report[8]:

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[3] Application, page 3
[4] Exhibit J1.1
[5] Exhibit J1.1
[6] Exhibit K1.2
[7] Page 31
[8] Pages 30-31

> The Board notes that there are clearly differences in perception as to the purpose of the incremental capital module. Ratepayer groups perceive the capital module as a mechanism aimed solely at addressing extraordinary or special CAPEX needs by distributors. The distributors, on the other hand, perceive the module as a special feature of the 3rd Generation IR architecture which would enable them to adjust rates on an on-going, as-needed basis to accommodate increases in rate base.
>
> In the Board's view, the distributors' view is not aligned with the comprehensive price cap form of IR which has been espoused by the Board in its July 14, 2008 Report. The distributors' concept better fits a "targeted OM&A" or "hybrid" form of IR. This alternative IR form was discussed extensively in earlier consultations but was not adopted by the Board. The intent is not to have an IR regime under which distributors would habitually have their CAPEX reviewed to determine whether their rates are adequate to support the required funding. Rather, the capital module is intended to be reserved for unusual circumstances that are not captured as a Z-factor and where the distributor has no other options for meeting its capital requirements within the context of its financial capacities underpinned by existing rates.

8. OPUCN has identified four projects which it asserts are outside its normal capital program and has provided evidence that the required funding for these projects would fall outside the capital spending threshold established by the Board. In VECC's view OPUCN has adopted an interpretation of the Board's Incremental Capital Adjustment module similar to VECC's. As a result, the balance of VECC's submissions deal with substance of the Application and whether the Utility has satisfied the Board's Filing Requirements.

FILING REQUIREMENTS FOR AN INCREMENTAL CAPITAL MODULE

OPUCN's Position

9. A distributor requesting an ICM adjustment as part of its 3GIRM rate application must meet specific filing guidelines which are set out in Appendix B (pages VI & VII) of the Board's September 2008 Supplementary Report. In its Argument-In-Chief OPUCN contended[9] that it had provided all of the information required and met the necessary requirements..

VECC's Submissions

10. Set out below are VECC's submissions regarding OPUCN's compliance with each of the Board's filing guidelines.

An analysis demonstrating that the materiality threshold test has been met and that the amounts will have a significant influence on the operation of the distributor

11. This requirement has two parts. The first is a demonstration that the materiality threshold has been met. In VECC view this requires that the utility demonstrate that all of the capital spending it is proposing for 2009 is non-discretionary (i.e., must be done in 2009) and that the spending in excess of the incremental capital threshold equal or exceeds the spending on the projects for which it is seeking funding. VECC submits that unless the utility can demonstrate that all of its proposed spending is non-discretionary the materially threshold is effectively meaningless and could virtually always be met by the utility including in its spending plans sufficient discretionary spending to trigger the threshold.

12. OPUCN contends that all of the projects it is proposing to do in 2009 are ones that it needs to do in 2009[10]. In support of this view, OPUCN filed an undertaking[11] which

[9] Volume #1, pages 133-135
[10] Volume #1, page 86

listed all of its Enhancement projects for 2009 and an explanation as to why each was considered non-discretionary. In the same exhibit, OPUCN noted that its 2009 spending on Expansions and Connections was mandatory under the requirements of the Distribution System Code.

13. VECC has reviewed the material provided and for most Enhancement projects the information provided supports their classification as "non-discretionary". However, there are a few cases where it is not patently clear that the projects need to be completed in 2009. Two examples of this are Project C08-211 (Conlin-Wilson to Harmony) and Project C08-203 (Harmony –Legend Centre to Conlin). In both instances the project's need is attributed to growth in the north-east part of OPUCN's service area[12]. However, there is no evidence that this growth is such that projects need to be completed this year. The combined cost of these two projects is slightly less than $600,000.

14. VECC notes that the cost of the four proposed projects ($2.2 M) which OPUCN is claiming as its incremental capital adjustment accounts for virtually all of the OPUCN's $2.3 M head room over the threshold value[13]. As a result, any determination that more than $100,000 of the total capital spending for 2009 is "discretionary" would reduce the dollars eligible for the incremental capital adjustment to a level below OPUCN's proposal.

15. With respect to the calculation of incremental capital threshold, OPUCN has applied the threshold formula as specified by the Board to derive a revised value of $6.7 M[14]. OPUCN has also reduced its 2009 capital budget by $1.5 M to account for carry-over from 2008. This results in potentially eligible spending of $2.3 M. VECC's comments on these calculations focus on the determination of the carry-over spending level.

16. During the course of oral proceeding OPUCN was asked about the 2008 under spending on wood pole placement and whether these funds ($346,700) could be

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[11] Exhibit J1.6
[12] Exhibit J1.6
[13] Exhibit J1.1
[14] Exhibit J1.1

considered as being available to help fund the concrete pole replacement program. OPUCN's witnesses responded that this under spending was accounted for in the 2008 "carry-over" adjustment.[15] However, in the undertaking response that details the projects carried over from 2008 the wood pole spending is not included[16]. This suggests to VECC that either the potentially eligible capital spending should be reduced by $346,700 (to account for this additional carry over) or the concrete pole project should be removed from the list of eligible projects on the basis that the necessary funds are already included in the base upon which the 2008 were set.

17. The second part of this filing guideline requires OPUCN to demonstrate that the spending will have a significant influence on its operation. In their opening comments OPUCN's witnesses asserted that the $285,000 in incremental revenue requirement was important to the Utility[17]. VECC notes that this represents over 1% of OPUCN's 2008 rebasing revenue requirement of roughly $20.6 M[18] and exceeds the 0.5% materiality threshold for Z-factors adopted by the Board for its 3GIRM[19].

A description of the underlying causes and timing of the capital expenditures including an indication of whether expenditure levels could trigger a further application before the end of the IR term

18. VECC accepts that OPUCN's evidence provides descriptions as to the underlying causes of its total capital program[20] as well as detailed descriptions for the four projects for which it is seeking relief using the incremental capital adjustment module.

19. OPUCN does not appear to have addressed the matter as to whether further applications would be triggered before the end of the IRM period.

An analysis of the revenue requirement associated with the capital spending (i.e., the incremental depreciation, OM&A, return on rate base and PILs

[15] Volume #1, pages 57-58
[16] Exhibit J1.3
[17] Volume #1, page 23
[18] OPUCN's 2009 Supplementary Filing Module, Tsb B3.1
[19] July 2008 3GIRM Report, pages 36-37
[20] Exhibit J1.6; VECC #5 and Board Staff #1

associated with the incremental capital), and a specific proposal as to the amount of relief sought

20. In Exhibit K1.2 OPUCN has provided a calculation as to the revenue requirement impact of the proposed capital spending that exceeded the threshold. VECC has no specific concerns regarding OPUCN's calculation of the revenue requirement associated with its proposed incremental capital adjustment.

Justification that amounts being sought are directly related to the claimed cause, which must be clearly non-discretionary and clearly outside of the base upon which current rates were derived. This includes historical plant continuity information for each year of the IR plan term since the last Board-approved Test Year.

Justification that the amounts to be incurred will be prudent. This means that the distributor's decision to incur the amounts represents the most cost-effective option (not necessarily least initial cost) for ratepayers.

21. These sections of the fling guidelines require an applicant to provide justification for the amounts claimed and demonstration that they are non-discretionary and prudent. In VECC's view the distinguishing feature between this requirement and first one discussed above is that this requirement focuses more specifically on the capital spending the Utility is seeking to include in its incremental capital adjustment and the details regarding the associated projects. In OPUCN's case there are four projects: a) Concrete Pole Replacement; b) Long Term Load Transfer Elimination; c) Distribution Reliability Improvement and d) Mobile Work Force[21]. The following paragraphs discuss each of these projects.

- *Concrete Pole Replacement*

22. The original application included a request for $1,521,800 in 2009 capital spending for concrete pole replacement and assumed the replacement of roughly 220 poles[22]. Following a more detailed inspection OPUCN determined that there were 30 poles that

[21] Application, page 4
[22] Application, page 6

required immediate replacement and revised its capital spending estimate for this project to $210,000[23]. In VECC's view OPUCN proposed 2009 spending on this project can be considered both non-discretionary and prudent.

23. VECC also notes that OPUCN's 2008 capital spending budget did not include any allowance for concrete pole replacement[24] and, therefore, the spending can be considered outside the current base upon which rates are set.

- *Long Term Load Transfer (LTLT) Elimination*

24. The application includes $907,500 to complete the elimination of all LTLT within the OPUCN territory in 2009[25]. In its Application, OPUCN contended that the project was "required by regulation and that the funding would permit OPUCN to complete removal of all long term load transfers within one year of the OEB deadline (January 31, 2009) rather than over several years[26]. The Utility also noted that its Application for extension on the deadline had so far not been accepted[27].

25. Subsequent to the Application, the OEB granted OPUCN's request for an extension on deadline to complete the removal of LTLT[28]. Also, prior to the start of the oral hearing, the OEB published a notice proposing amendments to the Distribution System Code that would extend the deadline for LTLT removal to June 30, 2014[29]. Despite these changes in regulatory requirements, OPUCN contends that it is still important to complete the LTLT removal in 2009[30]. The rationale given is improved reliability for the customers concerned[31].

26. VECC accepts that improved reliability is a contributing factor to the overall decision that OPUCN should build the necessary facilities to connect these customers and serve

[23] Board Staff #6
[24] Board Staff #3
[25] Application, page 8
[26] Application, page 9
[27] Application, page 7
[28] Board Staff #11
[29] Volume #1, page 15
[30] Board Staff #11 and Volume #1, page 16
[31] Volume #1, pages 17-18 and page 90

them on a permanent basis[32]. However, in VECC's view these same reliability considerations existed at the time of OPUCN's July 2008 request for an extension to deadline to 2011. Indeed the choice of 2011 (as opposed to 2012 as originally requested in June 2008) appears to be solely the result of a requirement by Hydro One Networks to have the project completed by that time[33]. Clearly reliability considerations at that time did not lead to OPUCN to consider completion of the removal of LTLT to be a non-discretionary project for 2009. Nor did the suggested improvements in reliability lead the Board to conclude that an extension should not be granted or the project completed over a shorter period.

27. VECC submits that no new information has been provided that would suggest the reliability concerns have escalated such that the project must now be considered as non-discretionary for 2009. Indeed, it appears the only reason this project has been advanced to 2009 is because the incremental capital module now provides funding for it[34]. As a result, it is VECC's submission that this project can not be viewed as non-discretionary for 2009.

- *Distribution System Reliability Improvement*

28. This project targets the replacement of a specific distribution feeder that has been identified as a poor performer and has an estimated cost of $850,000[35]. OPUCN's rationale for pursuing this project in 2009 is that by replacing a poor performing distribution feeder the overall reliability statistics of OPUCN will improve and that such results are consistent with the Board's findings in its 2008 Rate Decision[36]. During the oral proceeding, OPUCN witnesses also noted that there were worker safety issues associated with the current feeder due to sub-standard construction in comparison to current standards[37].

[32] Exhibit J1.5
[33] See relevant correspondence attached to Original Application.
[34] Volume #1, page 91
[35] Application, pages 10-11
[36] Application, pages 10-11
[37] Volume #1, pages 108-109

29. In VECC's view OPUCN has misinterpreted the direction of the Board from its 2008 Rate Decision. The Board did not say that OPUCN should increase capital spending in order to improve reliability. Rather the Board directed that in making decisions regarding capital spending OPUCN should ensure there is a resulting improvement in capital spending. In particular, it is VECC's submission that the Board Decision does not mean that any proposed spending that improves reliability must be considered as non-discretionary. VECC also notes that there are already a number of reliability-related projects in OPUCN's 2009 capital spending that are expected to make greater contribution to reliability improvement than the project targeted by the incremental capital application[38].

30. Having made this point, it appears that there may be safety issues associated with this feeder. However, this concern was not initially raised by OPUCN and only came up as result of questioning by Board Counsel. As a result, it is not clear to VECC that the situation is such that project must be considered as non-discretionary from this perspective.

31. Overall, it is VECC's conclusion that the project cannot be considered non-discretionary for 2009.

- *Mobile Work Force*

32. The purpose of this project is to automate the current processes used for creating work orders for field staff and capturing the records of work performed. The estimated cost of the project is $254,000[39]. OPUCN has provided[40] a summary of the business case for the project and, with a 3 year payback period, VECC concurs that the investment is prudent.

33. However, in VECC's view OPUCN has failed to demonstrate that the project is non-discretionary and <u>must</u> be undertaken for 2009.

[38] Volume #1, pages 62-63 and VECC #3 d)
[39] Application, pages 12-13
[40] Board Staff #16 b)

Evidence that the incremental revenue requested will not be recovered through other means (e.g., it is not, in full or in part, included in base rates or being funded by the expansion of service to include new customers and other load growth)

34. It is VECC's submission that OPUCN has failed to account for the fact that parts of the proposed capital spending are included in base rates and that incremental revenues/cost savings will arise from the proposed projects.

35. In the case of the Concrete Pole Replacement program VECC has already noted that the carry over allowance OPUCN has included in its calculation of eligible capital spending fails to account for the 2008 under spending/carry over work associated with wood pole replacement[41]. VECC notes that based on the revised 2009 budget for the Concreter Pole Replacement program this carry over is more than sufficient to fund the planned 2009 work[42].

36. In the case of the LTLT program there are minor incremental revenues that will arise from the increase in connected customers[43]. Similarly for the Distribution System Reliability Improvement project OPUCN has acknowledged that there will be O&M savings although OPUCN has not been able to quantify them[44].

37. Finally, in the case of the Mobile Work Force project OPUCN has indicated that the O&M savings will be sufficient to produce a 3-year payback[45]. OPUCN argues that it will take time for these savings to emerge[46]. However, in VECC's view it is reasonable to assume some level of savings over the next 3 years. At a minimum, VECC submits that savings should be assumed for the last half (i.e., 1 ½ years) of the IRM period.

A description of the actions the distributor will take in the event that the Board does not approve the application.

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[41] See preceding Paragraph #16
[42] Volume #1, pages 57-58
[43] Volume #1, page 107
[44] Volume #1, page 95
[45] Board Staff #16 b)
[46] Volume #1, pages 65-66

38. OPUCN has indicated that even if approval is not received for the incremental capital module funding the Utility will proceed with all of the projects except for the LTLT removal project[47].

Conclusion

39. In the first part of its argument VECC concluded that OPUCN's approach was consistent with the OEB's intent as to when the Incremental Capital Module should apply. However, as discussed above, there are a number of issues with OPUCN's specific Application. Summarized below are VECC's conclusions and recommendations – based on the submissions in the preceding paragraphs.

40. First the calculation of potentially eligible capital is overstated. The amount of potentially eligible capital should be reduced to $1.7 M[48] to account for the fact that not all of the 2009 capital program has been clearly demonstrated as being non-discretionary.

41. The Concrete Pole Replacement program should be considered as ineligible on the basis that the 2008 carry-over spending for the wood pole replacement program is more than sufficient to fund this project and this carry over spending has not been included in the derivation of "potentially eligible incremental capital spending".

42. The LTLT and The Distribution System Reliability Improvement projects should both be considered ineligible on the grounds that OPUCN has not demonstrated that the projects are non-discretionary for 2009. A supporting (but minor consideration) in both cases is the fact that there are incremental revenues/cost savings from these projects.

43. The Mobile Work Force project should be rejected as well on the basis that it is a discretionary project and the savings over the IRM period can be expected to cover a significant portion of the costs.

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[47] Volume #1, pages 99-100

[48] This represents a reduction of $600,000 and is based on the cost of the C08-203 and C08-211 capital projects. The carry over in spending on word pole replacement is addressed in conjunction with the eligibility of the concrete pole replacement program.

REGULATORY COSTS

OPUCN'S Position

44. OPUCN's incremental capital requirement application does not include the hearing costs (i.e., Board costs, legal costs or intervenor costs) associated with the Application. OPUCN proposes to recover these costs over a two year period[49]. The initial recovery would be based on a cost of $25,000 and a variance account would be established to track recoveries against actual costs[50].

VECC's Submissions

45. in its report on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, the Board stated[51]:

> A set of authorized variance / deferral accounts are identified in the Board's Accounting Procedures Handbook. In its December 20, 2006 "Report of the Board on Cost of Capital and 2nd Generation IR for Ontario's Electricity Distributors", the Board indicated that, to the extent possible, it will limit reliance on the creation of new deferral accounts during the term of the 2nd Generation IR plan to well-defined and well-justified cases only. The Board will continue this practice for purposes of the 3rd Generation IR plan.

The December 2006 Report of the Board also indicated that "Z-factor rules should govern need for, and treatment of deferral accounts[52].

46. The Board's 3GRIM Report indicates that for Utilities with a revenue requirement greater than $10 M but less than $100 M, the materiality threshold for Z-factors (and therefore also for deferral/variance accounts) is 0.5% of distribution revenues. OPUCN's distribution revenues are roughly $20 M which suggests a materiality threshold of $100,000. In VECC's view it is hard to imagine that the costs of proceeding will exceed this amount. Indeed, OPUCN's current forecast is for $25,000 in costs.

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[49] Volume #1, pages 16-17.
[50] Volume #1, page 136
[51] July 2008 Report, page 47
[52] Page 46

47. Based on these observations, it is VECC's submission that OPUCN's requests to include $25,000 for recovery of regulatory costs in the incremental capital adder and the establishment of an associated variance account should both be rejected by the Board.

COSTS

48. The Vulnerable Energy Consumers Coalition hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that the Vulnerable Energy Consumers Coalition has participated responsibly in all aspects of the proceeding, in a manner designed to assist the Board as efficiently as possible.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 4TH DAY OF MAY 2009