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October 22, 2009

VIA E-MAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto, ON
M4P 1E4

Dear Ms. Walli

Re: EB-2009-0243: Application for Recovery of Contact Voltage Remediation Costs Toronto Hydro Electric System Ltd

Please find enclosed the submissions of VECC in the above noted application.

Yours truly,

Original signed

Michael Buonaguro
Counsel for VECC
Encl.

EB-2009-0243 THESL Contact Voltage Cost Recovery Application

FINAL SUBMISSIONS OF VECC

SUMMARY OF SUBMISSIONS

1. VECC respectfully submits that the Board should refuse to grant the relief requested by the applicant in this proceeding.

2. In VECC's view there is a high onus on an applicant that seeks to interrupt an approved Cost of Service test year to reset rates to demonstrate that the an event truly exogenous to the obligations of the distributor to maintain its system has caused the utility to incur material incremental costs such that the utility could not reasonably be expected to operate without some incremental recovery. While VECC concedes that there may be situations that warrant such relief, VECC submits that the within application does not demonstrate that such a situation exists.

3. In VECC's respectful submission the Level III Emergency costs claimed by THESL resulted from THESL's operating decisions concerning the manner in which it decided to maintain its secondary distribution system, and not on any external cause that could ground a claim for relief.

4. To the extent that costs were incurred in connection with specific customer owned equipment or connections, VECC submits that THESL has failed to properly recover those costs directly from customers; in particular THESL has failed to directly allocate costs to its Affiliate THESI for repairs to THESI equipment.

5. Likewise, there is insufficient evidence to demonstrate that the incurred costs are incremental to THESL's 2009 operating costs.

6. Lastly, VECC opposes the THESL proposal to allocate any costs outside of the SEL and USL rate classes, on the basis that the evidence in this proceeding supports the finding that the costs were all incurred as a result of a need to detect, isolate and repair assets directly related to those two types of customers or used to serve only those two customer classes.

The characterization of the proposed costs as warranting a “Z-factor” recovery

7. At Page 1 of its Application THESL characterizes the nature of its application to recover costs related to Level III Emergency Costs:

> These costs were unforeseen and incremental to THESL’s existing approved revenue requirement. This Application is brought to demonstrate that these costs meet the eligibility requirements of the Board (Incrementality, Exogeneity, Materiality, and Prudence) pertaining to “Z-factor”-type costs and that recovery of these costs through rates is proper, just, and reasonable.

8. During the course of the oral hearing it was confirmed by THESL that it was relying on:

   a) the OEB Letter to Electricity Distributors Re: Wiring Faults", March 4th, 2009 (the “OEB Letter”), and

   b) the Report of the Board on 3rd Generation Incentive Regulation Mechanism for Ontario’s Electricity Distributors dated July 15, 2008[1] (the “Report”).

   as the regulatory bases for its application to recover costs.[2]

THE OEB LETTER

9. With respect to the OEB letter, THESL initially resisted the proposition that the letter was constrained to situations wherein THESL was required to step in and incur costs related to third party assets:

> MR. BUONAGURO: . . .
> That letter is specific to third-party assets and your stepping in to repair them; correct?
> MR. McLORG: I did not understand it that way. THESL did not interpret it that way.
> MR. BUONAGURO: Well --
> MR. McLORG: That letter essentially sets out the Board's expectation with respect to the conduct of business as usual or normal business.

[1] Along with the Supplemental Report of the Board issued on September 17, 2008
[2] Transcript Vol 1 page 73, 137

> The last paragraph specifically illustrates an exceptional departure from normal business.[3]

10. However, upon reviewing with THESL the text of the letter, it appears to VECC that THESL agreed that the subject matter was constrained to the repair of third party assets:

> MR. BUONAGURO: Mr. Millar was kind enough to give me his paper copy, although I am loathe to admit on the record that I am using a paper copy.
> The first sentence of that says:
> "The Board recognizes in some circumstances distributors may seek future recovery of the costs of repairs due to customer-owned equipment or connections."
> MR. McLORG: I see that.
> MR. BUONAGURO: So we are talking about -- this letter is in the context of the company having to go out and make repairs to customer-owned equipment or connections; right?
> MR. McLORG: I see what you are saying, yes.[4]

11. Accordingly (whether THESL ultimately agrees or not) VECC respectfully submits that the OEB Letter is very specific in what it a) expects from utilities and b) authorizes utilities to do, both of which are set out succinctly in the OEB Letter at page 2:

> It is expected that distributors have planned for, and are able to accommodate, all necessary maintenance or isolation of connections for unmetered loads to ensure the public's safety. In this regard, distributors are also expected to recover from the customer the cost of repairs or isolation of customer owned equipment or connections.
> A one-time billing charge or direct invoice may be used for this purpose. Distributors should where possible discuss in advance the need for correction to customer equipment.
>
> The Board recognizes that in some circumstances distributors may seek future recovery of the costs of repairs made to customer owned equipment or connections. In these circumstances distributors should record the appropriate amounts in deferral Account 1572 – Extraordinary Events Cost. Distributors may seek disposition of these accounts in conjunction with rate application filings. In seeking disposition distributors should be prepared to explain the amounts for which recovery is sought and what steps were taken to

[3] Transcript pages 72-73
[4] Transcript page 73

recover costs included in repairing the customer's connection or equipment.

12. The first paragraph above has no direct application to the within proceeding; it reinforces the expectation that distributors recover the cost of repair or isolation of customer owned equipment or connections directly from the customer. When handled in this way there is no need for further Board intervention.

13. The second paragraph may have application to the within proceeding, in that THESL may have repaired or isolated customer owned equipment or connections as part of the Level III Emergency Costs. To the extent such costs were incurred, the letter specifically directs the utility to seek disposition of those costs in conjunction with rate application filings, and in doing so outline the efforts made to recover the costs directly from the relevant customer.

14. THESL has not, obviously, followed the Board's direction in this regard, in that THESL is attempting to recover any such qualifying costs outside of a rate application.

15. More importantly, in VECC's view, it is not contemplated in the OEB letter that a utility would simply fail or be unable to track the 3rd party customer equipment or connections that it is repairing or connecting, which appears to be the case that THESL is advancing here.

16. With respect, it seems reasonable that in each instance where THESL encounters non-THESL equipment or connections that it could not locate owners for that it had the option of disconnecting the equipment in the normal course, as outlined in the letter, placing the onus on the owners to contact THESL for reconnection; VECC submits that such a scenario should be the rebuttable presumption that the Board operates under in such situations, and that THESL has failed to rebut that presumption in this case.

THE REPORT

17. THESL characterizes the identified costs as warranting Z factor treatment within the context of the Report, to the extent that when asked to concede that the Report does not strictly apply to THESL, THESL refused to make such a concession:

> MR. BUONAGURO: -- all of the costs in this application occurred in 2009?
> MR. McLORG: That's correct.
> MR. BUONAGURO: And for THESL, 2009 is the second year of a cost of service application?

> MR. McLORG: That's correct.
> MR. BUONAGURO: So 2009 is not an incentive regulation mechanism year for THESL?
> MR. McLORG: That's correct.
> MR. BUONAGURO: And no surprise to you, then, when I say, technically, the Board report on Z factors as they fit into a scheme of incentive regulation mechanisms doesn't strictly apply to THESL?
> MR. McLORG: No, I don't accept that. I don't think that there is anything in the Board's third generation report on IRM that specifically excludes utilities that are -- happen in that year to be under a cost of service rate-setting mechanism, and I would suggest to you that the underlying rationale for extending Z factor treatment is specifically to exempt extraordinary circumstances from the routine application of a given regulatory or rate-setting mechanism.[5]

18. THESL's refusal to concede that the Report of the Board on 3rd Generation Incentive Regulation Mechanism for Ontario's Electricity Distributors does not strictly apply to utilities that are not under 3rd generation persists even when confronted with indicia from the Report that specifies that the adjustments allowed in the Report are made on the basis of the 3rd generation IRM mechanisms:

> MR. SHEPHERD: Well, so you read a part of that, appendix B of that report, but you didn't read the beginning of appendix B. The beginning of appendix B says:
> "These filing guidelines set out the Board's expectations for applications by distributors for rate adjustments on the basis of the third generation IR mechanism."
> So the Z factor in here doesn't apply to you, does it?
> MR. McLORG: No, I don't accept that. It's a matter for argument, but I do not accept that.

19. THESL continues to assert that the Report applies to it even though it is not on an IRM, and even though it concedes that there are material differences in the COS and IRM regulatory structures:

> MR. BUONAGURO: Now, you mentioned storms specifically, and I may get back to that.
> Would you agree that a company going into a test year is in a different position than a company going into an IRM year in terms of its ability -- or, sorry, its right or -- I am not exactly sure how to characterize it, but going into that year, going into a test year, you have the opportunity to go through your expenses

[5] Transcript Vol 1 page 74-75

> and forecast them and accept the risk up or down on those specific items of risk?
> MR. McLORG: I can agree so far.
> MR. BUONAGURO: Right. And in an IRM, a company going into an IRM year doesn't have that opportunity, at least certainly not to the same extent. They accept the mechanical adjustment to their rates?
> MR. McLORG: I agree, yes.
> MR. BUONAGURO: So back in 2007 when you applied for rates effective 2008 and 2009, and in that application, 2010, I believe, you had the opportunity to forecast your budgets based on your view of what's going to happen in those test years and accept the risk, up or down, on whether your forecasts were accurate?
> MR. McLORG: I accept your statement with respect to business-as-usual items.[6]

20. VECC respectfully submits that Z factor treatment is accorded to utilities on Incentive Regulation Mechanisms to protect the utility (and shareholder) from diminished earnings and financial hardship related to unforeseen events outside of the control of management, largely in lieu of the fact that there is no opportunity for such utilities to forecast their expenses within the IRM year.

21. The regulatory compact under IRM recognizes that utilities operate in a relatively cost constrained environment due the productivity offset built into the IRM.

22. Accordingly there is little “wiggle room” to accommodate unexpected costs and therefore both Z-factors and Off-ramps are provided under IRM.

23. Toronto Hydro is <u>not</u> on an IRM. It has approved rates based on a two year Cost of Service (“COS”) Application EB-2007-0640 that set the Revenue Requirement and rates for 2008 and 2009. VECC notes that THESL originally sought a three year 2008-2010 COS approval.

24. VECC acknowledges that under COS, a utility can make application for new rates if it is able to prove it is materially under-earning relative to its approved ROE and, on the counter side the ratepayers or the regulator may call it in for a rate review(usually *ex post facto*), if its financial reports indicate excessive earnings.

25. The tests that apply for an application for new rates include the normal COS requirements of a forecast revenue deficiency in the current and/or future year.

[6] Transcript Vol1 Page 75 line 28 ff

26. The threshold for applying for new rates includes demonstration of actual or forecast under-earning. An application to change to existing rates due to a cost increase in part of the revenue requirement which is what THESL is de-facto seeking via rate riders, does not meet this test.

> MR. VLAHOS: It is not -- in my view, it's not a question of reopening, and I would not really allow, that to reopen all of the individual components that have led to the revenue requirement for the test year. But there is some questions by the intervenors as to: Is the company going to over earn for 2009? And, if that is the case, then should it be in addition to this that they should be recovering those Z factor costs?
> That is how I take some of the questions from the intervenors.
> MR. COUILLARD: Mr. Chair, if I may comment, the company is going to be far from over-earning this year. We are planning right now to be very close to what our operating expense -- I am not sure where Mr. Shepherd gets his number, and I would like to have the time to review them.
> But, you know, we are planning to be in line with our approved budget for operating, in line with our approved budget for capital, and we are about $20 million short on distribution revenue because of weather and because of the economy right now.
> So to make the conclusion that we are likely to overearn, I can state here today that we are not going to overearn this year.
> MR. VLAHOS: In the same vein, if it is not a question of over-earning, then do you think it is legitimate for the intervenors to pursue the question of to what extent the costs that may be materializing by the end of 2009 is a legitimate issue for the intervenors to pursue, if it is going to be way below or somewhat below what has been reflected in current rates.[7]

27. VECC submits that the evidence required to meet the test would be similar to THESL's 2010 COS Rate application, in essence a forecast material 2009 revenue deficiency that cannot be mitigated.

28. VECC submits that the only circumstance where a utility on COS rates may file an application to change rates (or seek approval of a rate rider) during a rate year without demonstrating a material revenue deficiency would be in the face of the unforeseen and major events resulting in extraordinary costs such as the 2003 Ice Storm and other Acts of God such as storm damage or new regulatory requirements such as smart meters; THESL acknowledges

[7] Transcript Volume 1 Page 128 line 11 ff

that there is no such event[8].

29. Even if there were such an event, the utility would normally apply for a deferral account to record the costs, which would then be subject to a prudence review in the next rates case. That review considers the incrementality of the costs and the impact on the historic and rate year earnings and ROE. That is not the case here:

> MR. BUONAGURO: I don't necessarily agree there is a Z factor, but I think you understand. You are applying for emergency Level III spending, and to the extent that there may have been avoided costs related specifically to that, you would have looked into that and put it into the application.
> MR. McLORG: Correct.
> MR. BUONAGURO: But you don't see that there are any.
> MR. McLORG: Correct. *<u>And just to be clear for the record, we also specifically did not go into a rendition of all of the other pluses and minuses that happen in our business in a normal year</u>*.(emphasis added)[9]

30. With respect to the key issue of whether any relief for THESL is appropriate related to the costs claimed for the Stray/Contact voltage Level III Emergency, VECC categorically answers *<u>NO</u>*.

31. The tests required for the relief that THESL is seeking (in year rate riders) simply have not been met. There is no evidence of reduced earnings as a result of the Emergency and the requested relief in the form of rate riders should be denied.

32. If THESL has the evidence that it needs the $14.35 million in order to avoid a 2009 revenue deficiency driven by the Level III emergency, it should have placed it in evidence in this case. Otherwise the remedy is to defer the costs and justify them when the 2009 Financial results are available as part of the 2010 Rates Case.

33. Accordingly, VECC suggests that the Board could consider allowing Deferral Account treatment of the Level III Emergency costs if THESL made such Application. Disposition of any amounts recorded would be subject to the Board's usual prudence review as part of the 2010 rates case, including:

a) A review of THESL's 2009 actual results in order to determine whether a material revenue deficiency due to the impact of the Level III Emergency occurred, including a review of the

[8] Exhibit J Tab 1 S 7 a)
[9] Transcript Vol 1 Page 44 Lone 24-Page 25 line 7

incrementality of the costs, particular the labour costs, with a view to assessing how the new work was managed within the existing resource base, and

b) a review of the causes of the costs as something warranting recovery beyond what has already been determined under the prevailing COS based rates.

34. If, however, the Board is inclined to consider the relief requested by THESL in the EB-2009-0243 Application, then VECC suggests that a number of major considerations bear on that decision:

- Cost Causality: are the costs incurred/caused by the utility as part of its regulated distribution activities
- Cost Attribution: are the costs appropriately divided between THESL and THESI and other Asset Owners?
- Prudence of the Costs: were the costs necessary and was cost control exercised?
- Incrementality of Costs claimed as Utility Costs: are these costs truly incremental to the approved cost of service and revenue requirement?
- Cost Allocation: are the utility costs allocated appropriately to the various classes based on principles of cost causality and the cost allocation model approved by the OEB, particularly in light of the Board's direction to recover these charges directly from customers?

Each of these factors are discussed below.

<u>Cost Causality and Cost Attribution</u>

35. The regulatory principle of cost causality requires that all of the costs claimed in Table 1 of THESLs written evidence were caused by the Level III emergency related to distribution of electricity in order to be recovered from utility ratepayers. The evidence on this is less than convincing.

36. The costs in Table 1 of its main evidence[10] are the portion of the total costs that THESL seeks to delineate as *utility costs*. Total costs incurred during the Level III Emergency include another $310,000 that THESI apparently incurred and THESL and THESI have decided these costs should be retained by THESI. The basis of this decision is not in evidence. What is in evidence is that both THESL and THESI crews responded to the level III Emergency situation[11], however there is no evidence as to the hours logged by each.

[10] Application Page 5 line 7
[11] Application Page 4 line 9ff

Remediation was carried out by THESL crews, THESI crews, and crews from available electrical contractors, all working under the direction of THESL management. Remediation work was itself undertaken in two categories; response to identified contact voltage incidents, and systematic inspection and repair, as necessary, of all handwells.

For identified contact voltage incidents, the first available crew from any of the labour pools was dispatched as soon as possible to the location to correct the faulty presence of voltage.

In cases where this involved equipment of THESL or THESI, the cause of the contact voltage was identified and corrected, [emphasis added] and any necessary repairs related to preventing its recurrence were made.[12]

37. With respect to the emphasized passage above, VECC notes that, apparently, THESL identified incidents of contact voltage that were caused by THESL or THESI equipment and made the necessary repairs to THESL and THESI equipment, but nowhere in the evidence does THESL explain how many of the contact voltage problems that were discovered were caused by THESL or THESI equipment.

38. The evidence is that out of the total labour costs of $ 5.92 million, including overtime, incurred by THESL and THESI crews[13] all except $280,000 was designated as utility costs. There is no evidence as to why THESI retained $280,000 of labour costs, while THESL retained $5.52 million of labour costs. Based on the number of incident reports[14] 401 events out of a total of 1640 (24%) were related to streetlighting assets owned by THESI. A direct allocation of labour costs based on incidents would result in $1.45 million being allocated directly to THESI rather than $280,000.[15]

39. The Board clearly recognized in its March 9, 2009 letter of direction to distributors that not all costs incurred due to stray voltage detection and remediation should be attributed to the utility and recovered from its ratepayers, directing that an attempt should be made to directly charge other asset owners for the costs that were reasonably incurred on their behalf.

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[12] Application Page 4
[13] Undertakings J1.1 and J1.2
[14] Undertaking J1.5
[15] During the hearing THESL testified that the fact that 401 events out of 1640 related to streetlighting assets did not mean the contact voltage problem was caused by those assets; however THESL provides no evidence as to how many of the 1640 incidents were caused by, as opposed to manifesting in, any particular group of assets.

40. In its letter of March 4, 2009[16], as noted above, the Board stated that

> It is expected that distributors have planned for, and are able to accommodate, all necessary maintenance or isolation of connections for unmetered loads to ensure the public's safety. In this regard, distributors are also expected to recover from the customer the cost of repairs or isolation of customer owned equipment or connections. A one-time billing charge or direct invoice may be used for this purpose. Distributors should where possible discuss in advance the need for correction to customer equipment.

41. THESL asserts that it did not have the data to properly charge these assets owners, but that the proposed Cost Allocation (see below) would result in a substantially similar result.

42. In VECC's submission, THESL has failed to make an adequate attempt to follow this direction of the Board; in particular, as noted above in the application, VECC notes that each contact voltage incident that was caused by THESL or THESI equipment was in fact identified and corrected, such that it should have been feasible to track the cost of those repairs and directly allocate costs, for example, to THESL's affiliate THESI.

43. THESL clearly believes that allocating the costs to the SEL and USL classes is a suitable proxy for directly allocating costs to specific customers:

> MR. SEAL: I think, in our evidence, we were clear in stating that based on the activities that we did in the Level III emergency, the tracking of those costs and knowing exactly who the customers were that were related to those particular assets that we had to remediate, was not possible.
> So we feel that the allocation that we have come up with is the fairest one.
> MR. BUONAGURO: But particularly with respect to USL, what that means is -- you can't tell who it is going to be because of the tracking problem, but there is going to be somebody in the USL class who is being charged the rider or would be charged the proposed rider even though none of their equipment was faulty. That's probable, unless you are saying that everybody in the USL class had at least one problem.
> MR. SEAL: That is not what we're saying.
> MR. BUONAGURO: Right.
> MR. SEAL: We are not saying that. In reality it is like any other costs that we do on the system.

[16] Application Appendix1

> If we go out and have to repair a particular residential customer service for whatever reason, that service doesn't necessarily get charged directly to them. It is part of the cost of the system. So, in this case, the USL we weren't able to identify it. The repairs we know were confined to those classes almost totally. And the allocation methodology that we proposed, we think is the fairest one we can come up with.[17]

44. It is true that these parties (or their service providers) are customers in the SEL and USL Classes. However THESL has not demonstrated that a direct attribution/allocation to individual asset owners (as the Board directed) of costs incurred during the Level III Emergency would be the same as using the cost allocation model that makes a cost allocation based on the number of the connections in each class.

45. VECC notes here, to be discussed later on, that in developing its proxy of allocating costs to the SEL and USL classes rather than directly charging costs to customers as they were directed to do by the Board, that THESL has refused to use the same logic in charging the scanning costs to those same classes; accordingly one ends up with the intuitively unfair result of charging to residential and small GS customers approximately 86% of the costs of searching for contact voltage problems[18], despite the fact that THESL is confident that "the repairs we know of were confined to those [SEL and USL] classes almost totally.[19]

The Causes of the Emergency Costs were not Exogeneous

46. The actual, physical causes of the contact voltage problems were all, in VECC's respectful submission, causes that were either under the direct control and management of THESL, one of its affiliates (THESI) or some other third party such that even if the THESL qualifies for Z Factor type applications analogous to what is contemplated by the Report, THESL has not demonstrated that the costs were truly exogenuous such that it qualifies for relief.

47. Throughout the application the causes of the contact voltage problems are described as resulting from:

a) missing plastic caps, degraded or faulty insulation, and improper repacking of the conductors,[20]
b) more generally, wear and failure of assets nearing the end of their life cycle,[21] and

[17] Tr Vol1 Page 57 Line 4 ff
[18] Application page 10.
[19] Transcript page 57.
[20] Application pages 6-7

c) bifurcated ownership and control of secondary distribution plant.[22]

48. THESL specifically conceded that there was no single event that costs the applied for costs,[23]and that it has never had a specific maintenance program for its secondary system, despite having a specific maintenance program for every other part of its system.[24] THESL conceded that it runs the secondary system on a "run to failure" basis.[25]

49. VECC respectfully submits that the combination of factors described above with respect to the causes of the problems show that the costs were caused by THESL's operating decisions with respect to the affected assets, decisions for which it bears the risk.

50. THESL asserts that its decision to not specifically maintain the secondary system was based on their assessment of the relative risk of failure on the secondary system and the corresponding danger to the public of such a failure.[26]

51. Yet despite the criticality of THESL's assertion as to the reasonableness of its failure to specifically maintain the secondary system, it has not provided any evidence with respect to any analysis it performed that resulted in the conclusion that failures on the secondary system were benign from a public safety standpoint.

52. This failure in the evidence is particularly disturbing in light of the fact that THESL admits that prior to the year 2006 it had recorded three incidents of contact voltage. THESL concluded that those incidents were "one-offs", even though it concedes that it did not review or investigate the incidents to determine if they were indeed "one-offs".[27]

53. VECC respectfully submits that the culmination of contact voltage problems and related costs in 2009 was not the result of an exogenous cause such that THESL may qualify for relief. It is VECC's submission that the causes were related to THESL's maintenance obligations in the normal course of their duty as the distributor, and that the operating decisions made by THESL in determining how to properly maintain its assets as they approached their end of life, along with the choices THESL made in assessing the safety risk associated with failures in the system.

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[21] Exhibit J Tab 2 S 1 d) and e)
[22] Exhibit J Tab 1 S 3 c)
[23] Exhibit J Tab 1 S 7 a)
[24] Transcript pages 142-144
[25] Transcript page 162
[26] Transcript pages 143-147
[27] Transcript page 45.

54. VECC asserts that the consequences of THESL's plan of action leading up to 2009 is highlighted by the fact that when they did, in fact, begin the review their secondary system and related contact voltage issues they discovered that 9.7% of their handwells required corrective repair or asset replacement[28], and that there were in excess of 1500 existing conditions of contact voltage.[29]

Incrementality of Costs Claimed as Utility Costs

55. This issue relates to whether the costs claimed in Table 1 of the application are prudently incurred and truly incremental to the approved cost of service and revenue requirement.

56. VECC submits that to properly to answer these issues it is necessary to see the total picture regarding the actual vs. approved 2009 Cost of Service, which goes back to the threshold issue of the type of relief THESL is seeking at mid-year 2009.

57. In this application THESL has only provided anecdotal evidence that the Level III costs were and are incremental. With the possible exception of the Services of the specialized Stray Voltage Scanning Contractor, there is little basis for THESL to claim that the labour costs were incremental (particular since $3.37M of the labour costs were regular time and therefore already included in rates[30]) and equally importantly it has not demonstrated that there are no offsets other than those discussed by Mr. La Pianta [31]available from other parts of its 2009 Operating and/or Capital Budget:

> MR. McLORG: Yes. Toronto's position would be that the net incremental cost of a Z factor event is the portion of it that is eligible for recovery, if you can make that case otherwise.
> MR. BUONAGURO: But you would not agree with the proposition, for example, that if the emergency Z factor costs are X and you reallocate resources towards it, but, as it turns out, there are offsets in other areas that you don't actually have to incur additional costs to accommodate the Z factor, you are saying, Well, that's too bad for ratepayers?
> You are saying if we had $10 million to pay for the emergency event but it turns out we had $10 million available under our revenue requirement, because our revenue requirement was $10 million more than we actually were going to spend anyway, it doesn't matter, unless it is linked specifically to the Z factor?

28 Exhibit J Tab 1 S 4 b)
29 Undertaking J 1.5
30 Exhibit J1.2
31 Tr Vol 1 Page 39 line 6 ff

> MR. McLORG: There has to be a specific linkage to the Z factor. The application brought by Toronto Hydro does not comprehend a thorough resetting of the 2009 revenue requirement, and it is not an opportunity to reopen what the Board has already approved.[32]

58. VECC submits that situating the costs claimed to be incremental in comparison to the test year revenue requirement is one of the critical reasons that, for example, in the case of the OEB Letter, the applicant is directed to file for recovery in the subsequent application filing.[33]

59. An application such as this one by THESL is essentially a claim that some intervening exogenous event has caused the utility to incur costs that are material such that the prevailing 2009 revenue requirement that is approved in rates is insufficient; in making such an application THESL is, in fact, seeking to re-open its 2009 rate order.

60. With regard to ongoing street level stray voltage scanning costs (in 2009 post-emergency and 2010) it is not by any means clear that this O&M cost cannot be accommodated in the 2009 operating budget by reducing/deferring other costs. This issue has not been tested in this case and would properly be a matter to address in the 2010 rates case, where evidence relating to 2009 can be reviewed.

Cost allocation and 2009 Rate Riders

61. The costs claimed by THESL in Table 1 [34] include Level III emergency costs (detection and remediation) and (post emergency) ongoing street level scanning for Stray/Contact Voltage.

62. THESL proposes to allocate the Level III Emergency Remediation costs ($7,790,000) to Ratepayers in the Street lighting and Unmetered Scattered Load classes.[35] based on the number of connections, THESL states that the justification for this allocation is that it produces a result that is similar or substantially the same as a direct allocation:

> MR. BUONAGURO: I would like to talk about the remediation costs first. My understanding from your evidence -- I am going to paraphrase and you can correct me if I am wrong, but there is a letter from the Board talking about situations

[32] Tr Vol 1 Page 43 Line 21 ff
[33] Application Appendix 1, page 2. VECC further notes, as an aside, that the Report, at Appendix B page V, for the purposes of recovering Z Factors, that IRM applicants are directed to file for relief in their next rate filing.
[34] Application Page 5 line 7
[35] Application Exhibit 1 Derivation of Rate riders filed June 30,2009 (All the Emergency costs other then scanning)

where you have to go out and do repairs to third-party equipment, and you have included it in your evidence.

MR. McLORG: That's right.

MR. BUONAGURO: Generally the policy is, if you are out there to fix third-party equipment, they pay for it directly, if you can get that paid.

MR. McLORG: That's correct in the normal course of business, Mr. Buonaguro.

If there is a specific incident in which the owner of the asset is readily identifiable and has probably entered discussions with Toronto Hydro as to the nature of the defect that needs to be corrected and the costs that will be consequential there to, then those charges are, as a matter of normal business, assessed against the asset owner.

MR. BUONAGURO: Because presumably it is because it is their assets that cause the need for the repair in the first place, a problem with third-party assets.

MR. McLORG: That is a fair statement generally, yes.

MR. BUONAGURO: I am going to paraphrase your evidence and you can correct me if I am wrong, but basically what you explained to us through your evidence and IRs is that you are not doing it that way directly getting it per customer per asset, because the scope of the undertaking was such that you didn't have the facility to track every asset repair.

So instead as a proxy for what the Board wants you to do, you are proposing to allocate those costs to the streetlighting in USL classes because that is where the costs reside in the first place. It is their assets -- you would be recovering from those ratepayers in any event.

Therefore, allocating those costs to those classes is almost the same as getting it directly from them, those costs.

MR. McLORG: In the end the result is the same, approximately.

I don't think that the two questions are directly related, as was implied in your question. Because our practice, concerning the recovery of costs for customer-owned equipment in the normal course, is as I stated. And there is no question of allocation around that.

Whereas your question seemed to imply that we were somehow departing from, quote, what the Board wanted us to do.

In our proposal, because of the circumstances that are that are explained in detail in our application, the best proxy that we can suggest is that the remediation costs be allocated proportionally to the connections on a secondary equipment for

each of the USL and SL rate classes. I am sorry, Mr. Seal, I am taking words out of your mouth, aren't I?
MR. SEAL: That is correct.[36]

63. However, THESL proposes to allocate the entire costs of scanning in 2009 ($6,555,000) to all customers based on the number of connections served at secondary voltage. This brings in an allocation to the residential and GS< 50 kw classes. THESL asserts that this manner of allocation is appropriate because these are system-wide costs incurred to check the total system for stray voltage.

64. VECC disagrees. The evidence is that the ongoing scanning is undertaken by mobile units to check for stray voltage along all streets. However in the City of Toronto the main connections on the street/boulevard are those related to Streetlights, Traffic Signals and control units, Bus shelters and BIA assets that are in the SEL and USL classes.

65. To allocate these costs outside of the SEL and USL classes, including the Residential class, using the number of connections on secondary as the allocator is in VECC's submission simply wrong and has no basis in cost causality.

66. With respect, the Scanning Program is concentrated on scanning street level assets that are for the most part in the SEL and USL classes, or assets that may be subject to contact voltage as a result of the secondary distribution system that services the SEL and USL class assets. The mere fact that the secondary system exists throughout the franchise area does not alter the reality that it is a distinct system to which the costs of scanning should be allocated based on the principle of cost causality:

MR. SHEPHERD: Although the scanning system, the scanning program is indiscriminate, in fact you have the scanning program for the secondary system. Don't you?
MR. LaPIANTA: Well, no. I don't think that is fair. I think we have the scanning program to protect the public on the boulevard because it is not just scanning the secondary.
MR. SHEPHERD: No. I understand that. But the thing you have to inspect, the thing that you have identified as a problem that you feel that you now have to inspect that you didn't before is the secondary system; right?
MR. LaPIANTA: Correct.[37]

[36] Transcript pages 54-56
[37] Transcript page 163

67. While it is no doubt important to detect contact voltage problems in order to promote public safety, that is not the relevant factor in determining who should pay for the cost of detection. The cost of detection should be borne by those causing the contact voltage problems, and therefore putting the public at risk, creating the need for the scanning.

68. In the first instance this would be done by directly charging those customers whose equipment are causing the problems; in the second instance, failing direct charges, VECC asserts that it is appropriate to allocate the costs to the classes who are served by the assets causing the problems. In either case, there is no evidence that the cause of contact voltage problems are assets owned by or use to serve any class outside of SEL and USL customers.

69. It appears to VECC that some of the confusion in the hearing of this issue results from how THESL presented the results of the scanning process. It appears to VECC that while the scanning process detected in excess of 1500 instances of "contact voltage", and that contact voltage could manifest itself in just about any type of asset (awnings, street poles, bus shelters, etc.), and that exhibit J1.5 illustrates where contact voltage manifested itself, the records kept in conjunction with the scanning provide no information as precisely what asset(s) required repairs:

> MR. McLORG: It could also be that our language in answering this interrogatory was unfortunate, because our interpretation of the question put by Energy Probe - innocently, I might add - was that it was intending to seek information on where the contact voltage was found.
> And perhaps that is our fault by responding with the same word, but -- because you know, for example, we had to interpret it, in our minds, to a plausible view, because a streetlight pole by itself is not a source of voltage. So it would be technically inaccurate to portray it as a cause of contact voltage, because it doesn't generate any voltage.
> It can exhibit contact voltage, but what the point of my qualification here is simply to say that there is no solid ground here upon which to attribute causation in the normal sense that we do in a ratemaking context.
> MR. BUONAGURO: For the purposes of scanning costs specifically; is that what you mean?
> MR. McLORG: What I am suggesting is that the answer that is given to Energy Probe in Interrogatory 2 is not indicative of the underlying cause of the contact voltage that was discovered.[38]

[38] Transcript pages 65-66.

70. The remediation costs, on the other hand, relate entirely to the cost of actually correcting the causes of the contact voltage, either through the inspection and repair of handwells or through the follow up repairs relating to issues detected by the scanning; in either case THESL is proposing that all of the actual repair costs are properly attributable to the SEL and USL classes as a matter of cost causality.

71. In VECC's view this can lead to only one reasonable conclusion; that the vast majority of contact voltage instances that made scanning necessary were caused by assets related specifically to the service of electricity to either the SEL or USL classes.

72. Accordingly if the Board finds that any part of the ongoing scanning costs are eligible to be recovered from ratepayers, VECC urges the Board to find that the principles of cost causality apply to the scanning costs in the same way THESL applies those principles to the Level III Emergency remediation costs such that any scanning costs should be allocated to the SEL and USL rate classes.

73. The results of such an allocation have been provided in the corrected response to Board staff IR#7[39].

Ongoing Scanning Costs-Sole Source Contract

74. Following the Level III emergency (ended in March 2009) THESL has entered into a multi-year sole source contract with Power Survey Corporation:

> MR. BUONAGURO: So you didn't tender the second one. You would agree, I think, that you are supposed to under normal circumstances when it is not an emergency, but you seem to be telling me that, Even if we had tendered, they would be the only person to apply?
> MR. LaPIANTA: That's correct. The sole source policy or provisions at Toronto Hydro allow us to entertain a vendor which, in our opinion, provides the service that we are seeking to retain and allow us to enter into negotiations with that vendor to come to fruition to a contract.
> The prices that we negotiate on an ongoing basis, given our different needs, are different from what we sustained during the emergency Level III.[40]

75. Undertaking J 1.4 provides information about THESL's decision to sole source the post-emergency scanning to PSC. The undertaking request was to

[39] Exhibit K1.1 revised Exhibit J Tab3 Schedule 7 Appendix A
[40] Transcript Page 50 line 8 ff

provide documentation relating to the selection of PSC as the sole source vendor for continued scanning expenditures; VECC notes that the only documentation that was provided in response to the undertaking was (other than the actual contract) a summary prepared specifically for the Undertaking response, rather than the production of any documents outlining the process and decisions made by THESL in concluding that PSC should be sole sourced.

76. In VECC's view the documentation supporting the sole sourcing of PSC is insufficient. On the plus side PSC uses the latest proprietary technology to detect Stray/Contact voltage using mobile antenna arrays and has been accepted by several US jurisdictions. On the negative side there are other contractors offer similar services. The Issue is whether THESL and its customers are getting the best value for money from the PWC sole source contract.

> MR. FAYE: Is this all being done by this one company?
> MR. LaPIANTA: To the best of my knowledge, again, Power Services Company is the only approved company by the Power Services Commission of the State of New York. There is only one other company -- I think this goes to the question this morning about our due diligence. There is only one other company that we know of which, I don't need to mention here, but they have not been approved, have tried on a number of occasions to be approved by a number of regulatory bodies in the US and have not been successful. So to the best of our knowledge, there is only this one vendor right now. Moreover, there is intellectual property proceedings, if you will, against the only other potential vendor of this technology. So we were not about to actually entertain going down that path with someone was not approved, who didn't have the experience or background as the company we entertained.[41]

77. In the absence of a tender, or alternatively a comparison of costs with those of US utilities, there is inadequate support to satisfy the value for money requirement, particularly when THESL proposes to retain such services over the foreseeable future at a cost of several million dollars a year. The onus of proof is on THESL to show that tendering is not feasible and VECC submits that it has not met this burden of proof.

78. As a consequence, the Board should not accept the PSC contract as the appropriate measure of the reasonable cost of scanning on a yearly basis, either in the context of the amount claimed in this proceeding or in the context of the amount claimed in future proceedings. THESL should be required to provide further and better evidence that properly supports sole sourcing this

[41] Transcript Vol1 Page 122 line 28 ff

contract, or tender the contract.

Summary

79. Based on the evidence filed by THESL and adduced in the hearing, THESL has not met the threshold burden of proof required under Cost of Service Regulation to justify the in year recovery of costs related to the Level III Stray/Contact Voltage Emergency. VECC submits that THESL is not entitled to apply for Z Factor relief in accordance with the Board's Report. VECC concedes that THESL can, as a utility under an existing COS rate regime, apply to the Board for relief under exceptional circumstances, but submits that those circumstances have not been demonstrated in this case.

80. VECC submits that if the Board is persuaded that THESL may be entitled to consideration of its Application, such consideration should be deferred and in the interim THESL should be directed to track the costs in a deferral account for consideration in either the current 2010 rates case or subsequent rates case.

81. If the Board is inclined to consider the Application in this proceeding, then several major deficiencies in the evidence make determination of the quantum of costs to be recovered and from which parties, including ratepayers, extremely difficult/arbitrary.

82. THESL has failed to demonstrate that in accordance with the Board's Letter of March 9, 2009, the costs cannot be attributed at least in part, directly to those asset owners that caused them. VECC suggests that based on incidents, it is clear that the parties owning the majority of assets involved are affiliates or related parties of THESL such that at least some significant portion of the costs could have been directly allocated to specific customers.

83. THESL has not demonstrated that the costs were incurred as a result of events outside of THESL's control; in VECC's submission the costs that were incurred were caused primarily by THESL's failure to maintain or plan for the maintenance of end of life assets, failed to proactively maintain its secondary distribution system at all, and failed to properly assess the risk posed by that lack of maintenance.

84. THESL has failed to demonstrate that the costs claimed are truly incremental to its 2009 revenue requirement as a result of having failed to file evidence relating to 2009 spending, and more specifically having failed to bring this application within the context of its next general rate filing.

85. THESL has failed to demonstrate that the sole source contract with PSC provides the best value for money. THESL should be required either to tender

the contract or on the alternative provide a comparison of costs with those of other US utilities.

86. In the event that the Board determines that THESL is entitled to recover costs in this application, and that such costs should be allocated to customer classes and recovered in rates, VECC submits that while it may be appropriate, in the face of a legitimate inability to directly charge the appropriate customers, to allocate all the remediation costs to the SEL and USL classes based on number of connections, it is **not** appropriate to allocate scanning costs to all customer classes and applying number of connections as the cost allocator.

87. VECC submits that there is no basis in cost causality for the allocation of scanning costs outside of the SEL and USL classes. There is no evidence that the need to perform scanning, either on an emergency basis or otherwise is related to something other than assets that are the cause of stray/contact voltage problems, thereby requiring scanning to determine where contact voltage is occurring to allow the tracking of problem back to the cause for remediation. The Board should reject THESL's proposition and require that any and all costs eligible for recovery be allocated based on connections in the Street and Expressway Lighting and Unmetered Scattered Load Classes.

All of which is respectfully submitted this 22nd day of October, 2009