Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

December 11, 2009

MIDDLESEX POWER DISTRIBUTION CORPORATION

ELECTRICITY DISTRIBUTION RATES
DUTTON HYDRO LIMITED

EB-2009-0177

Introduction

Dutton Hydro Limited ("Dutton Hydro") is a licensed electricity distributor serving approximately 600 customers in the Village of Dutton. On February 9, 2009, the Board approved Middlesex Power Distribution Corporation's ("Middlesex Power") acquisition of Dutton Hydro and Newbury Power Inc. (EB-2008-0332). As part of the record of that proceeding, it was noted that Dutton Hydro's rates have not been adjusted since 2001. Middlesex Power and Dutton Hydro proposed to file a 2006 cost of service application for the Dutton Hydro service area based on a 2004 historical text year and IRM adjustments for 2007, 2008 and 2009. This process would bring Dutton Hydro to the same level as Middlesex Power and Newbury Power Inc. in preparation for rate rebasing on a merged basis in 2014.

Middlesex Power filed the Dutton Hydro rate application on June 11, 2009, and subsequently updated the application on June 29, 2009. The application proposed a Mitigation Plan as the total bill impacts exceeded 10%. No parties responded to the Notice of Application. On October 21, 2009, Middlesex Power filed responses to Board staff interrogatories. Middlesex Power informed the Board that in the course of preparing interrogatory responses, Middlesex Power discovered that the distribution rates charged by Dutton Hydro to its customers since May 1, 2005 are not Board-approved rates. On November 3, 2009, Middlesex Power filed a proposed Mitigation Plan to refund amounts overcharged from May 1, 2005 to December 31, 2009. The plan was subsequently updated on November 13, 2009.

This submission reflects observations and comments which arise from Board staff's review of the pre-filed evidence and interrogatory responses provided by Middlesex Power. Generally, the Board staff submission is limited in focus, commensurate with the evidence.

The Application

The application, as filed on June 29, 2009, provided the following bill impacts from the 2006 cost of service application based on a 2004 historical text year and IRM adjustments for 2007, 2008 and 2009.

Bill Impact	Delivery		Total Bill	
	2006-2009	**2006-2009 with Mitigation Plan**	**2006-2009**	**2006-2009 with Mitigation Plan**
Residential (1,000 kWh)	110.7%	31.4%	33.3%	11.0%
GS < 50 kW (2,000 kWh)	123.1%	29.5%	31.5%	9.3%

The bill impacts associated with the Mitigation Plan filed on November 13, 2009 are the same as those associated with the Mitigation Plan filed on June 29, 2009.

2006 Cost of Service

The Applicant filed the 2006 EDR model to establish rates based on the 2004 historical test year. The EDR model indicates a proposed revenue requirement of $187,305. The table below shows a breakdown of the base revenue requirement.

Distribution Expenses	$177,105
+ Return on Rate Base	$31,697
+ PILs	$0
Service Revenue Requirement	$208,802
- Revenue Offset	$21,497
Base Revenue Requirement	$187,305

The Applicant has four customer classes. The proposed numbers for customers and their associated load for 2004 are shown in the table below.

2004	Number of Customers	kWh per Customer	kW per Customer
Residential	484	9589	
GS<50	82	45,529	33.8
Sentinel Light	1	940	1.0
Street Light	1	138,310	305.0

Rate Base

Staff notes that the 2004 fixed asset accounts conform for the most part to balances filed previously with the Board. Staff notes that the Applicant reported total net fixed assets as of December 31, 2004 of $320,664 with a working capital allowance calculation based on 15% of cost of power and controllable expenses of $101,777. The Applicant's reported rate base is $422,441.

<u>Tier 1 Adjustment – Rate Base</u>

The Applicant seeks a Tier 1 adjustment of $8,500 related to PCB elimination and $40,000 related to replacement of poles. In its response to interrogatory #6, the Applicant provided a pole assessment completed by Utility Scanning Solutions in June 2008. The analysis indicated that 15 of 56 poles tested should be replaced. Transformer PCB analysis was also conducted in June 2008. The analysis indicated that 3 of 24 transformers tested require replacement. Staff notes that this work does not technically meet the Tier 1 rate base criteria listed on page 12 of the 2006 EDR Handbook, e.g. new transformer stations with in-service date of <u>2005</u>. However, staff notes that this application for 2006 cost of service is filed in 2009 and that the type of expense and the level of expense is reasonable and supported by the evidence.

Distribution Expenses

Staff notes that the 2004 OM&A accounts conform for the most part to balances filed previously with the Board. The Applicant confirmed in response to interrogatory #9 that Dutton Hydro did not have any employees at any time. During the period 2002 to 2009, all of the maintenance and administration services were provided by the Village of Dutton/Dunwich. Billing and collecting services were provided by Enwin Utilities from 2002 to 2005 and by Chatham Kent Utility Services from 2006 to 2009. The year to year trends in distribution expenses for these services are irregular, ranging from -31% to 33% for the 2002 to 2004 period and ranging from -45% to 124% in the 2005 to 2009 period. Middlesex Power was unable to provide comments on the trends as the Dutton Hydro records relating to expense rationale are limited. Subject to staff's comments below on Tier 1 adjustments, the Board may wish to consider accepting the proposed 2004 distribution expense level of $177,105 for rate setting purposes in light of the fact that the amalgamation will undoubtedly result in improved record keeping by the new owners going forward and that the new owners will monitor distribution expense trends and provide rationale for trends in future rate applications.

Tier 1 Adjustment – Distribution Expense

In addition to the standard adjustments allowed by the 2006 EDR model, the Applicant proposed two Tier 1 adjustments.

The Applicant proposed a Tier 1 adjustment related to ESA fees and low voltage charges. Interrogatory #5 queried the $3,500 expense related to ESA fees. The Applicant replied that the fees became effective after 2004 and that they proposed recovery as a non-routine expense. The expense does not technically meet the Tier 1 distribution expense criteria listed on page 12 of the 2006 EDR Handbook, i.e. non-routine/unusual for 2004 only. However, staff note that this application for 2006 cost of service is filed in 2009 and submit that the nature of the expense and the level of the expense is reasonable.

The application also proposed a Tier 1 adjustment of $15,000 related to low voltage charges. In response to interrogatory #13, the Applicant provided the details of low voltage charges for the period 2002 to 2004. Based on a recalculation, the Applicant has determined that the low voltage adjustment should be $11,377 and not $15,000. The Applicant confirmed that there is no low voltage charge in current rates. Staff submit that the adjustment of $11,377 is reasonable.

Cost of Capital

Based on the 2006 EDR Handbook, a 50/50 debt/equity capital structure is appropriate as the Applicant has net fixed assets of less than $100 million. The Applicant has also requested IRM adjustments for 2007, 2008 and 2009, and a movement from 50/50 to 56.7/43.4 debt/equity capital structure. Staff notes that the Applicant proposed a weighted average cost of capital of 7.50% based on a 56.7/43.3 debt/equity split. The Board may wish to consider that the k factor adjustment embedded within the IRM models for 2008 and 2009 is meant to transition the 2006 starting point for the capital structure from the 50/50 split to 56.7/43.3. This has been the approach used in rate applications to transition utilities towards the common capital structure of 60% debt and 40% equity, consistent with the *Report of the Board on Cost or Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors*, issued December

20, 2006. In its reply submission the Applicant may wish to clarify its proposed capital structure in sheet 3-2 of the 2006 EDR model. Using a 50/50 debt/equity split, staff has calculated the weighted average cost of capital to be 7.62%. The Applicant may wish to confirm this in its reply submission.

The Applicant states that it currently does not have any actual debt and requests a deemed debt rate of 6.25%, consistent with the Board's 2006 long term debt rate for small distributors (with a rate base of less than $100 million). The ROE used was the Board's approved rate in 2006 of 9.00%. Staff has no concerns with this part of the Applicant's proposal.

Revenue Offsets

Board staff has no concerns with the revenue offsets proposed for the 2004 test year. With respect to the Specific Service Charges, staff notes that the Applicant has chosen the standard charges for all activities. The total revenue offsets are made up of $5,226 from Specific Service Charges, $2,909 from Late Payment and $13,362 from Other Distribution Revenue, mostly made up from retail service charges.

Allocation and 2004 Billing Determinants

Staff has no concerns with the historical 2004 load. The Applicant has appeared to follow the 2006 EDR methodology for normalizing the 2004 load to be used as the billing determinant and the allocation of the base revenue requirement to the classes and for establishing the fixed/variable charges; likewise for the low voltage expense.

Payments in Lieu of Income Taxes

In response to Board staff interrogatory #10, the Applicant states that it does have loss carry forwards which are greater than the target net income found on Schedule 4-1 of the 2006 EDR model. The Applicant noted that it is in the process of verifying the amount with the Ministry of Finance. The Applicant estimates the payment in lieu of taxes to be nil and they have not filed the tax model.

The Applicant also noted the following:

> "The loss carry forward is being applied to the future taxable income which is being estimated to be zero due to taking into account the loss carry forward. Therefore,

> there will not be any PIL's recovered in rates which is a benefit to the customers. At the time of the next rate rebasing any potential loss carry forward will be provided and will again reduce payment in lieu of taxes being recovered from the customers."

The Board may wish to consider accepting the nil PILs proxy for rate setting purposes as proposed by the Applicant but staff notes that the Board consider this to be an approval on a final basis. In the event that the Ministry of Finance finds that there is tax owing for the applicable period, this would be the responsibility of the shareholder.

Loss Factor

In the application update filed on June 29, 2009, the Applicant proposed a supply loss factor of 1.034, a distribution loss factor of 1.0611 and a total loss factor of 1.0951. The Applicant is only able to provide data for the years 2007 and 2008 to support its application for the high loss factor. The total loss factor for 2007 and 2008 is reported as 1.0972 and 1.0929 respectively. The application states that, "[Dutton Hydro] has not done any upgrades to the Distribution System for several years."

Board staff interrogatory #12 observed that a total loss factor of 1.05 is noted in the 2006 EDR model, but a total loss factor of 1.0662 is listed as the current loss factor in the IRM Rate Generator Model. The interrogatory sought the data to support historical loss factors. In their response, the Applicant stated that, "the information is unavailable from the previous owners."

Board staff submits that the loss factor proposed is unreasonably high. Dutton Hydro lacks records that could be analysed for loss factor trends. Accordingly, staff suggest that little confidence can be placed in the 2007 and 2008 data. For comparison, examples of total loss factors that have been approved for small distributors would include Hydro 2000 Inc. at 1.066 (EB-2007-0704) and Rideau St. Lawrence Distribution Inc. at 1.076 (EB-2007-0762). Dutton Hydro's 2007 and 2008 loss factor data suggest metering inaccuracies and/or an inordinately high number of unmetered loads.

Board staff interrogatory #12 also sought a detailed loss factor mitigation plan, as required by the 2006 EDR Handbook for distribution loss factors greater than 5%. In response the Applicant stated that some investments in switch replacements and transformer upgrades will be made and some equipment will be relocated to eliminate tree contacts. The Applicant stated that investing in monitoring systems will provide the data necessary to analyze and optimize the distribution system to improve losses. Board staff does not understand the relationship between tree contacts and line losses. Staff recommends that the Board set the deemed total loss factor at 6.62%. The setting for the total loss factor at over 9% would be unprecedented and there is simply no reliable evidence supporting this number. The lower 6.62% is found in the IRM models and appears to represent the currently applied total loss factor. Regardless, staff notes that any variances between actual and deemed loss factors are tracked in account 1588 Power. Staff also recommends that the Applicant be directed to file a plan to reduce distribution losses with the next cost of service application as Hydro 2000 was directed to file in its 2006 decision (RP-2005-0020/EB-2005-0380). Hydro 2000 subsequently filed a study titled the Utility Load Flow and Evaluation Study for the EB-2007-0704 proceeding.

Regulatory Asset Recovery

The Applicant is requesting disposition of balances as of December 31, 2004, in RSVA accounts 1580, 1582, 1584 and 1586 and in account 1508. The balances, which also include Hydro One charges during 2005, are set out below. These data were provided in the continuity schedule provided in response to interrogatory #14. Staff notes that this is the first instance in which the Applicant has requested recovery of its regulatory asset balances since market opening.

Account Number	Account Description	Principal Balance
1580	RSVA – Wholesale Market Service Charge	$24,812
1582	RSVA – One-time Wholesale Market Service	$1,018
1584	RSVA – Retail Transmission Network Charge	$2,233
1586	RSVA – Retail Transmission Connection Charge	$111,943
1508	Other Regulatory Assets	$3,355
	TOTAL	**$143,361**

As noted in the continuity schedule, the principal balance above with interest to December 31, 2009 amounts to $163,620.

The Applicant's plan is to obtain approval for the amounts to be recovered, but to delay the timing of the recovery to the next IRM period as part of the Mitigation Plan filed on

June 29, 2009 discussed below. The Mitigation Plan, with respect to regulatory assets, was subsequently updated on November 13, 2009.

Interrogatory #14 requested that the Applicant complete a continuity schedule and to determine rate riders assuming recovery of December 31, 2008 balances with interest to January 1, 2010. The Applicant replied to this interrogatory with an updated interest calculation but the response indicated no further transactions beyond those listed in the table above.

Board staff note that there is no known reason why principal transactions beyond 2004 would not have occurred. It is unclear to Board staff whether this is simply an option chosen by the Applicant in order to defer additional bill impacts in the near term or whether transactions beyond 2004 are not available. As noted above, billing and collecting services for the Applicant were carried out by Chatham-Kent Utility services between 2006 and 2009. It is therefore reasonable to assume that Chatham-Kent Utility services also carried out settlement activities with the IESO and Hydro One. If so, it is unclear to Board staff why this information would not be available to the new owners. Regardless, staff invite the Applicant in its reply submission to clarify the status of the post 2004 transactions. The Applicant should not introduce new evidence at this stage. The clarification is for context only. As for the matter of the 2004 balances, Staff recommends that the Board accept the proposed balances for disposition. Staff notes that if balances beyond the 2004 period become available they may be brought forward for review and disposition at a future rate application.

Smart Meter Adder

In the application filed in June 2009, the Applicant proposed a $1.00 smart meter rider to minimize the impact of full deployment of smart meters in 2010. The application noted that Dutton Hydro was purchased by Middlesex Power and that the latter is one of the 13 distributors authorized to undertake smart metering activities. Middlesex Power will install the smart meters for Dutton Hydro customers in 2010.

Board staff wish to clarify that the request should be for an adder, not a rider.

The Applicant has requested that the implementation of the smart meter charge should be delayed to the 2010 IRM process as part of the Mitigation Plan discussed below.

Retail Transmission Service Rates

In the original application, the Applicant filed for a uniform increase of 11.3% for the network charge and 5.5% for the connection charge. These percentage increases are consistent with the Board's Guideline *Electricity Distribution Retail Transmission Service Rates [G-2008-0001]* issued on October 22, 2008. The Applicant has requested that the RTSR increases be deferred to the next application as part of the Mitigation Plan discussed below.

Board staff notes that the guideline was revised on July 22, 2009 to reflect the Decision and Rate Order in proceeding EB-2008-0272, setting new Uniform Transmission Rates for Ontario transmitters, effective July 1, 2009. The guideline also noted that transmission rates will change on January 1, 2010. Accordingly, staff submit that the requested increases are not appropriate. In addition, while the Applicant has recorded a large debit balance in its retail transmission connection variance account (1586) as of December 31, 2004, there is no updated information on this balance in this application. In light of the Applicant's wish to defer the implementation of RTSR increases, staff suggests that the current level of RTSRs remain in place and that the Applicant apply for RTSR adjustments as part of its 2010 IRM application. The revised filing guidelines should be followed for that application.

IRM

The Applicant has applied for a mechanistic and formulaic IRM process for the years 2007, 2008 and 2009. The Applicant requests the price escalator less a productivity factor (X-factor) of 1% for each of the three years.

Board staff submits that the request is reasonable and that the Applicant has entered the correct data and implemented the mechanics of the IRM models appropriately.

Rate Mitigation Plans

The application as filed on June 29, 2009 would result in the total bill impact of 33.3% for a residential consumer (1,000 kWh) and 31.5% for a GS<50 consumer (2,000 kWh). The Applicant proposed a mitigation plan consisting of deferral of low voltage charges, regulatory asset recovery, smart meter adder and RTSR adjustments to the next rate application. The Applicant determined that the bill impacts would drop to 11.0% for a typical residential consumer and to 9.3% for a typical GS<50 consumer.

In the course of preparing interrogatory responses, Middlesex Power discovered that the distribution rates charged by Dutton Hydro to its customers since May 1, 2005 are not Board-approved rates. On November 3, 2009, Middlesex Power filed a proposed Mitigation Plan to refund amounts overcharged from May 1, 2005 to December 31, 2009. The plan was subsequently updated on November 13, 2009.

The Applicant has determined that the amount overcharged from May 1, 2005 to December 31, 2009 is calculated to be $82,353. The Applicant has estimated the final months of 2009, and Board staff submit that the estimate appears to be reasonable. The Applicant proposes to return the amount overcharged through an offset of regulatory asset recovery. The Applicant proposes to recover $82,353 in regulatory assets through a volumetric rate rider and return $82,353 to customers through a volumetric credit rider in this application. Accordingly, the Applicant stated that the bill impacts are the same as noted above. The Applicant proposes to recover the remaining regulatory asset balances i.e. $81,267 ($163,620 - $82,353) over a two year period to begin with the next rate application. The Applicant states that the proposal will not materially impact consumers beyond the 10% threshold. Staff submit that the proposal is reasonable.

EDR Model Updates

Staff has noted certain changes made by the Applicant to the 2006 EDR model filed with the original application over the course of this proceeding. Staff notes that the Applicant should file an updated 2006 EDR model and 2007, 2008 and 2009 IRM models with its reply submission clearly mapping any changes made to the established evidence.

All of which is respectfully submitted