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Ontario

BY EMAIL

February 1, 2010

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

Dear Ms. Walli:

Re: Board Staff Submission on London Hydro Inc.
2010 Electricity Distribution Rates Application
Board File Number EB-2009-0235

Please see attached Board staff's submission for the above proceeding. Please forward the attached to London Hydro Inc. and any intervenors in this proceeding.

London Hydro Inc. reply to submissions is due February 22, 2010.

Yours truly,

Original Signed by

Martin Benum
Advisor, Applications and Regulatory Audit

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2010 ELECTRICITY DISTRIBUTION RATES

London Hydro Inc.

EB-2009-0235

February 1, 2010

Board Staff Submission
London Hydro Inc.
2010 IRM3 Rate Application
EB-2009-0235

Introduction

London Hydro Inc. ("London Hydro") filed an application with the Ontario Energy Board (the "Board"), received on October 19, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that London Hydro charges for electricity distribution, to be effective May 1, 2010. The application is based on the 2010 3rd Generation Incentive Regulation Mechanism.

The purpose of this document is to provide the Board with the submissions of Board staff based on its review of the evidence submitted by London Hydro.

Board staff makes submissions on the following matters:

- Potential Tax Sharing Rate Rider;
- Disposition of Deferral and Variance Accounts as per the Electricity Distributors' Deferral and Variance Account Review Report (the "EDDVAR Report");
- Adjustments to the Revenue to Cost Ratios;
- Adjustments to the Retail Transmission Service Rates; and
- Accounting for the implementation of the Harmonized Sales Tax ("HST").

POTENTIAL TAX SHARING RATE RIDER

General Background

The Supplemental Report of the Board on 3rd generation incentive regulation issued on September 17, 2008 determined that a 50/50 sharing of the impact of currently known legislated tax changes, as applied to the tax level reflected in the Board-approved base rates for a distributor, is appropriate. The calculated annual tax changes over the plan term are to be allocated to customer rate classes on the basis of the Board-approved base-year distribution revenue. These amounts will be collected from or refunded to customers each year of the plan term, over a 12-month period, through an explicit volumetric rate rider derived using annualized consumption by customer class underlying the Board-approved base rates.

London Hydro Specific Background

Using the Board's Supplemental Filing module, London Hydro's Tax Sharing amount is a refund of $251,005. This amount when unitized using London Hydro's volumetric billing determinants results in energy-based kWh rate riders less than four decimal places and demand-based kW rate riders less than two decimal places.

Submission

Board staff notes that as a result of having kWh Tax Sharing rate adders of $(0.0000) when rounded to the fourth decimal place and kW Tax Sharing rate adders of $(0.00) when rounded to the second decimal place, the refund amount of $251,005 will not be returned to ratepayers, which defeats the intent of tax sharing process. Board staff submits that the Board may wish to consider directing London Hydro to record the Tax Sharing refund amount of $251,005 in the variance account 1595 for disposition in a future rate setting.

DISPOSITION OF DEFERRAL AND VARIANCE ACCOUNTS AS PER THE EDDVAR REPORT

General Background

For purposes of 2010 IRM applications, the EDDVAR Report requires a distributor to determine the value of its December 31, 2008 Group 1 Deferral and Variance account balance and determine whether the balance exceeded the preset disposition threshold of $0.001 per kWh using the 2008 annual kWh consumption reported to the Board.

When the preset disposition threshold is exceeded, a distributor is required to file a proposal for the disposition of Group 1 account balances (including carrying charges) and include the associated rate riders in its 2010 IRM Rate Generator for the disposition of the balances in these accounts. The onus is on the distributor to justify why any account balance in excess of the threshold should not be cleared.

Any distributor exceeding the preset disposition threshold was required to file a Deferral and Variance Account Workform.

London Hydro Specific Background

Annual Disposition

London Hydro has not exceeded the disposition threshold as reported in its initial filing and therefore did not complete and file the Board staff Deferral and Variance Account Workform. Board staff interrogatory #1 requested that London Hydro complete and submit an updated version 4 of the Deferral Variance Account Workform. London Hydro complied with this request. The completed model confirmed that London Hydro's Group 1 account balance did not exceed the preset disposition threshold of $0.001 per kWh.

Submission

Board staff submits that London Hydro has complied with the filing requirements of the 2010 Deferral Variance Account Workform and has demonstrated that it is not required to dispose of its Group 1 account balances.

ADJUSTMENTS TO THE REVENUE TO COST RATIOS

Background

The Board's Decision (EB-2008-0235) for London Hydro's 2009 cost of service rate application prescribed a phase-in period to adjust the revenue to cost ratios. The 2010

Supplemental Filing Module included schedules for London Hydro to complete to address this matter. The process adjusts base distribution rates before the application of the price cap adjustment.

Submission

Board staff submits that London Hydro has complied with the filing requirements of the 2010 Supplemental Filing Module. Board staff takes no issue with London Hydro's revenue to cost ratio adjustments.

ADJUSTMENTS TO THE RETAIL TRANSMISSION SERVICE RATES (RTSR)

General Background

Electricity transmitters in Ontario charge Uniform Transmission Rates (UTR) to their transmission connected customers. These UTRs are charged for network, line connection and transformation connection services. Based on the Decision and Rate Order of the Board in the EB-2008-0272 proceeding, the new UTRs effective July 1, 2009 were as follows:

- Network Service Rate was increased from $2.57 to $2.66 per kW per month, a 3.5% increase;
- Line Connection Service Rate remained unchanged at $0.70 per kW per month; and
- Transformation Connection Service Rate was decreased from $1.62 to $1.57 per kW per month, for a combined Line and Transformation Connection Service Rates reduction of 2.2%.

On July 22, 2009 the Board issued an amended "Guideline for *Electricity Distribution Retail Transmission Service Rates*" ("RTSR Guideline"), which provided electricity distributors with instructions on the evidence needed, and the process to be used, to adjust Retail Transmission Service Rates ("RTSRs") to reflect the changes in the UTRs effective July 1, 2009. The Board set as a proxy at that time an increase of 3.5% for the

Network Service Rate and reduction of 2.2% for the combined Line and Transformation Connection Service Rates. The Board also noted that there would be further changes to the UTRs in January 2010.

Based on the Decision and Rate Order of the Board in the EB-2008-0272 proceeding, a Rate Order issued January 21, 2010 revised the UTRs effective January 1, 2010 as follows:

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

London Hydro Specific Background

London Hydro's Manager Summary stated that its "existing RTSR's as approved by the Board in its Rate Order issued on September 22, 2009 EB-2008-0235, have been adjusted for the changes to the whole transmission rates effective July 1, 2009. London Hydro is not requesting or proposing any further changes to RTSR's in this application."

Submission

Board staff notes that London Hydro effected in their 2009 rates the July 1, 2009 level of UTRs. Board staff submits that London Hydro RTSR rates may no longer be reasonable, based on the January 1, 2010 level of the UTRs. Board staff submits that the applicant's proposed rates be revised to reflect the incremental change from July 1, 2009 to January 1, 2010 values by applying an adjustment of 11.7% for Network and 7.5% for Connection RTSR rates.

ACCOUNTING FOR THE IMPLEMENTATION OF THE HARMONIZED SALES TAX

General Background

The Ontario provincial sales tax (“PST”) (currently at 8%) and the Federal goods and services tax (“GST”) (currently at 5%) will be harmonized effective July 1, 2010, at 13%, pursuant to Ontario Bill 218 which received Royal Assent on December 15, 2009.

The PST is currently an incremental cost applied to the price of goods purchased by an electricity distributor and is included in a distributor’s OM&A expenses and capital expenditures. The PST is therefore included in the distributor’s revenue requirement and is recovered from ratepayers through the application of distribution rates.

When the PST and GST are harmonized, distributors will pay the HST on purchased goods and service but will now claim an input tax credit for the PST portion. The mechanics of HST as a value added tax means that the distributor will no longer incur that portion of the tax that was formerly applied as PST (i.e. the 8%) on goods purchased. However, the current rates as applied will continue to effect cost recovery as if the PST was still in place. If no action is taken, the distributor will realize a savings in the cost of goods purchased while applying rates which do not reflect those savings.

London Hydro Specific Background

In response to Board staff interrogatory # 6a which asked if London Hydro agrees that a deferral account should be established to capture the reductions in OM&A and capital expenditures, London Hydro stated that it “does not agree or concur with the Board’s proposal that the avoided PST should somehow be quantified and captured in a deferral account for future disposition.” London Hydro emphasized that it “would be inherently unfair for the Board to narrowly focus their attention on one specific cost element engrained in rates, while at the same time electing to ignore the reality that many other cost elements will be subjected to cost increases. If we are to seriously consider the Board's proposal we should not ignore the fact that effective July 1, 2010 all billings issued by LDC's will increase by an additional 8% as a result of the tax harmonization. This change will increase accounts receivable and reduce available working capital thus placing further strain on utility cashflows."

Further London Hydro stated that "what the Board is proposing, if it were to be carried out, would require an enormous administrative process and expense."

Lastly, London Hydro noted that for "those utilities that have filed their cost of service rate applications prior to 2010, what the Board is proposing is in essence, retroactive ratemaking on a very selective basis."

Submission

Board staff notes that many distributors' comments on the administrative burden and costs of sales tax harmonization are at odds with the provincial and Federal governments' pronouncements regarding the stimulative and competitive results of harmonization. Because the costs and savings are not clear at this point, Board staff submits that tracking of these is warranted at this point to quantify, per government pronouncements, that the potential savings for corporations like London Hydro could be significant. Accordingly, Board staff submits that the Board may wish to consider establishing a deferral account to record the amounts, after July 1, 2010 and until London Hydro's next cost-of-service rebasing application, that were formerly incorporated as the 8% PST on capital expenditures and expenses incurred, but which will now be eligible for an HST Input Tax Credit ("ITC"). The intention of this account would be to track the incremental change due to the introduction of the HST that incorporates an ITC from the 5% to the 13% level. To qualify for this treatment, the cost of the subject items must be in the category of distribution revenue requirement. Tracking of these amounts would continue in the deferral account until London Hydro's next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

London Hydro would apply to clear the balance in the account as a credit to customers at the next opportunity for a rate change after the account balance information becomes available and is supported by audited financial statements.

All of which is respectfully submitted