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BY EMAIL

February 1, 2010

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

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

**Re: Board Staff Submission on Waterloo North Hydro Inc.
2010 Electricity Distribution Rates Application
Board File Number EB-2009-0210**

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

Waterloo North 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

Waterloo North Hydro Inc.

EB-2009-0210

February 1, 2010

**Board Staff Submission
Waterloo North Hydro Inc.
2010 IRM2 Rate Application
EB-2009-0210**

Introduction

Waterloo North Hydro Inc. ("Waterloo North") filed an application with the Ontario Energy Board (the "Board"), received on October 20, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that Waterloo North charges for electricity distribution, to be effective May 1, 2010. The application is based on the 2010 2nd 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 Waterloo North.

Board staff makes submissions on the following matters:

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

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.

Waterloo North Specific Background

Annual Disposition

Waterloo North has requested the disposition of its Group 1 account balance. Waterloo North stated that it “is proposing a four year disposition period in its repayment of its Group 1 Deferral and Variance Account Balances. Waterloo North Hydro has chosen this disposition period to protect its customers from rate shock that would occur if the entire balance was disposed of during one rate year. If disposition occurred over one rate year, customers would appreciate the large decrease the first year, however, they would be subsequently shocked to see such a large increase the following year. Waterloo North Hydro has chosen four years in order to minimize rate shock, afford its customers lower rates for four years than they would otherwise have, and reflect the number of years over which the majority of the balances were accumulated.”

Board staff interrogatory #4 requested that Waterloo North complete and submit an updated version 4 of the Deferral Variance Account Workform. Waterloo North has complied with this request.

Global Adjustment

In response to Board staff interrogatory # 1a, Waterloo North stated it had reviewed the Regulatory Audit & Accounting Bulletin 200901 and confirmed that it had accounted for its Account 1588 RSVA power and global adjustment sub-account in accordance with this Bulletin. In response to Board staff interrogatory #1b, Waterloo North confirmed that it made an immaterial (0.2% of total amount for applied for disposition) adjustment to its carrying charges subsequent to its initial application to comply with the Regulatory Audit & Accounting Bulletin 200901 with respect to account 1588 and the global adjustment sub-account.

In response to Board staff interrogatory #2a, Waterloo North agreed that a separate rate rider be prospectively applied to non-RPP customers to dispose of the global adjustment sub-account balance would be appropriate on the basis of cost causality. In response to Board staff interrogatories #2b, Waterloo North stated that it did currently have the billing capability to have a separate rate rider applicable to non-RPP customers to dispose of the global adjustment sub-account balance.

As of November 1, 2009 the MUSH sector (Municipalities, Universities, Schools and Hospitals) and other designated institutional customers that remained as RPP customers were required to switch to non-RPP customer status as per O. Reg. 95/05 of the Ontario Energy Board Act, 1998. In response to Board staff interrogatories #3d, Waterloo North indicated that the rate rider should not apply to RPP customers, and should exclude customers in the MUSH sector. Waterloo North further indicated that it "is capable of excluding the limited number of MUSH customers being applied with this separate rate rider; however, extensive modifications would have to be made to the WNH billing system by its software provider."

Waterloo North have requested that the Board review and approve the disposition of the December 31, 2008 balances of other Group 1 Deferral and Variance accounts as defined by the EDDVAR Report. The total balance of the Group 1 accounts, excluding the 1588 global adjustment sub-account is a credit of \$14,671,135. The 1588 global adjustment sub-account balance is a debit of \$984,306. Waterloo North has included interest, using the Board's prescribed interest rates, on these account balances up to April 30, 2010. Debit balances are amounts recoverable from customers.

Waterloo North did not address any concern with respect to the impact on its cash flow were it to use the one-year default disposition period contemplated in the EDDVAR Report to clear its deferral and variance account balances. Waterloo North did select a 4-year disposition period in its Deferral Variance Account Workform V4 for the reason as noted in the Manager's Summary reported above.

Submission

Board staff suggests that the Board may wish to consider establishing a separate rate rider for the disposition of the global adjustment sub-account balance. The rate rider would apply prospectively to non-RPP customers, and would exclude the MUSH sector and other designated customers that were on RPP. Board staff submits that recovering the global adjustment sub-account balance solely from non-RPP customers would be more reflective of cost causality since it was that group of customers that were undercharged by the distributor in the first place. However, the Board may wish to consider, as an alternative, to recover the allocated global adjustment sub-account balance from all customers in each class. This approach would recognize the customer

migration that might occur both away from the non-RPP customer group and into the non-RPP customer group.

In addition to the decision on whether a separate rate rider should be established for the disposition of the global adjustment sub-account, the Board must decide on the time period over which the rate riders should apply. As previously noted, customer migration might occur in the low volume group. For this group of customers, there would be a benefit to dispose of the global adjustment sub-account balance over a relatively short period of time in order to reduce inter-generational inequities. Board staff submits that a disposition period no longer than one year would be appropriate. These balances have been accumulating over the last four year period and to delay immediate action is not in the customer's best interest. Board staff recognizes that some volatility in electricity bills [may](#) result. That aside, Board staff believes that a one year disposition period would be in the interest of all parties.

In order to reduce inter-generational inequities, Board staff submits that the disposition period for all Group 1 accounts should not exceed one year.

The EDDVAR Report includes filing guidelines for the disposition of deferral and variance account balances. With respect to the reliability of account balances, the EDDVAR Report at page 27 states "...The Board believes that ...additional audit certification is not necessary. The Board however will require a distributor to file a reconciliation of the regulatory trial balance that is reported to the Board as part of RRR and the audited financial statements."

Board staff notes the original balances proposed for disposition (and supported by audited financial statements) might have been adjusted to account for events subsequent to the release of the EDDVAR Report. They include, but are not exclusive to the following:

1. The Regulatory Audit & Accounting Bulletin 200901 ("accounting bulletin") dated October 15, 2009 and accounting frequently asked questions issued in October 2009 clarified the accounting rules for account 1588 RSVApower and global adjustment sub-account. The accounting bulletin required electricity distributors to review and correct misstatements since January 1, 2005 or since the last time Account 1588 RSVApower and global adjustment sub-account were cleared by

the Board on a final basis. Due to the changes to account balances arising from the accounting bulletin Board staff asked distributors to confirm their compliance to the accounting requirements specified in the bulletin.

2. Applicants retroactively reviewing, and correcting Group 1 account balances over the January 1, 2005 to December 31, 2008 period.

Board staff notes that the final proposed balances for disposition may no longer reconcile with previously audited balances nor with Waterloo North's RRR filings. Board staff has reviewed the balances and notes that the changes do not result in material differences. Board staff notes that Waterloo North stated in response to staff's interrogatory # 4c that Waterloo North has complied with the Board's accounting policies and procedures. Board staff is mindful of the importance of a timely disposition of deferral and variance account balances and does not believe that the disposition should be delayed. Board staff suggests that the Board consider approving the proposed deferral and variance account balance disposition rate riders on a final basis.

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.

Waterloo North Specific Background

Waterloo North has applied for an adjustment to its RTSR rates based on the July 22, 2009 RTSR Guideline proxy rate adjustments.

Submission

Board staff notes that very few distributors, including Waterloo North, effected in their 2009 rates the July 1, 2009 level of UTRs since for most of them, distribution rates would have been implemented on May 1, 2009. Therefore, in accordance with the July 22, 2009 RTSR Guideline, Board staff submits that the revisions to the RTSRs ought to reflect the changes from the current level to the January 1, 2010 level, that is an increase of about 15.6% to the RTSR Network Service rate, and an increase of about 5.2% to the RTSR Line and Transformation Connection Service Rate.

Board staff has reviewed the evidence provided and submits that the proposal of Waterloo North 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 January 1, 2010 values.

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.

Waterloo North Specific Background

In response to Board staff interrogatory # 5a which asked if Waterloo North agrees that a deferral account should be established to capture the reductions in OM&A and capital expenditures, Waterloo North stated it "does not agree with the establishment of a variance account to capture the reductions in OM&A and capital expenditures..."

Waterloo North submitted that it "will have its rates for May 1, 2010 set under the 2nd Generation IRM policies. WNH's rates will continue to be based on the 2004 historical test

year, they will not be based on a forward test year. As such, WNH recommends that distributors with rates set under 2nd Generation IRM not be subject to the establishment of a variance account.”

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 Waterloo North 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 Waterloo North’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 Waterloo North’s next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

Board staff acknowledges Waterloo North’s comments that its base rates were set using the 2004 historical test year. Board staff however submits that the revenue requirement for the 2004 historical test year would also have included PST amounts for capital expenditures and expenses. As such, Board staff does not understand why this should warrant a different treatment.

Waterloo North 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