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Ontario

BY E-MAIL

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 Norfolk Power Distribution Inc.
2010 Electricity Distribution Rates Application
Board File Number EB-2009-0238**

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

Norfolk Power Distribution Inc. reply to submissions is due February 22, 2010.

Yours truly,

Original Signed By

Martin Benum
Advisor, Applications and Regulatory Audit

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2010 ELECTRICITY DISTRIBUTION RATES

Norfolk Power Distribution Inc.

EB-2009-0238

February 01, 2010

Board Staff Submission
Norfolk Power Distribution Inc.
2010 IRM3 Rate Application
EB-2009-0238

Introduction

Norfolk Power Distribution Inc. ("Norfolk") filed an application with the Ontario Energy Board (the "Board"), received on October 21, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that Norfolk 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 Norfolk.

Board staff makes submissions on the following matters:

- Z-Factor – Storm Damage Costs;
- Disposition of Deferral and Variance Accounts as per the Electricity Distributors' Deferral and Variance Account Review Report (the "EDDVAR Report");
- Potential Lost Revenue Adjustment Mechanism ("LRAM") and Shared Savings Mechanism ("SSM") rate rider(s);
- 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").

Z-Factor – Storm Damage Costs

General Background

Z-factors are intended to provide for unforeseen events outside of management's control, and are a common feature of IR plans. The costs to a distributor of these events must be material, prudently incurred, and its cost causation clear.

Pursuant to the Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, dated July 14, 2008 ("3rd Generation IRM"):

- Distributors are expected to report events to the Board promptly and apply to the Board for any amounts claimed under Z-factor treatment with the next rate application. This will permit the Board and any affected distributor to address extraordinary events in a timely manner. Subsequently, the Board may review and prospectively adjust the amounts claimed under Z-factor treatment.

- The Board expects that any application for a Z-factor will be accompanied by a clear demonstration that the management of the distributor could not have been able to plan and budget for the event and that the harm caused by extraordinary events is genuinely incremental to their experience or reasonable expectations.

Pursuant to the Board's Decision with Reasons for the Combined Proceeding On Storm Damage Cost Claims dated July 31, 2007 (EB-2007-0514 ,EB-2007-0595 ,EB-2007-0571,EB-2007-0551),the Board makes some general remarks on issues that were of a general nature to provide some guidance to applicants, Board Staff and stakeholders on the regulatory treatment of future storm damage cost claims.

Materiality

> The Board expects that distributors will exercise good judgement on whether or not claims should be filed, even if the costs incurred pass the materiality threshold.

Insurance and Reserves

With materiality, accounting procedures and capitalization practices firmed up, the Z- Factor mechanism is preferable at this time to mandatory insurance in that it provides a reasonable expectation that prudently incurred costs are recoverable, where they can be shown to be genuinely incremental to costs already embedded in rates.

Tracking Storm Damage Costs

On a go-forward basis and as the industry routinely rebases, it is the Board's expectation that distributors will identify a forecast for storm damage costs within their greater O&M forecast.

Reporting Requirements

The Board does expect distributors to forecast the revenue that they will likely receive for assisting other distributors, in the same way as they factor in rates a provision for normalized annual storm damage costs.

Norfolk Specific Background

On January 14, 2007 an ice storm hit the service territory of Norfolk. Approximately 87% or 16,080 out of 18,500 customers were without power, some for as long as 33 hours. To aid in restoring power, Norfolk obtained the assistance of neighbouring utilities, external contractors as well as its own staff (incurring overtime). Norfolk crews worked for 3 days to restore power to the County followed by an additional week to clean up (including tree trimming and damaged plant replacement).

On November 16, 2007 Norfolk filed a cost of service application for rates effective May 1, 2008 (EB-2007-0753). Within its application, Norfolk made a request to recover $213,851 of costs caused by the ice storm. The Board denied Norfolk's request based on insufficient evidence to support its claim. The Board noted that any further requests to dispose of this amount be supported by an analysis of the historic spending on storm damage that has been built into the revenue requirement on which the current rates are based. The Board also noted that it would be helpful if a comparative analysis of the spending levels attributable to storm damages be included in a future application.

In this application, Norfolk requested the recovery of a Z-factor relating to the storm damages that occurred in January 2007 in the amount of $179,448. Norfolk is requesting that the amount be recovered by a volumetric rate rider over the period of one year, beginning May 1, 2010.

A detail breakdown of the expenses to be recovered is as follows:

Description	**Amount**
Internal Labour (including overtime)	$47,684
Materials	$11,102
LDC's and external Contractors	$132,270
Trucks & Equipment	$8,630
Special Accommodations & Meals	$2,063
Total Costs Related to Ice Storm	**$201,749**
Adjustments	
Less: Non-incremental internal labour	-$28,884
Less: Non-incremental Trucks & Equipment	-$8,630
2007 Ice Storm Incremental Expense	**$164,235**
Carrying Charges	$15,214
Total Costs to be Recovered	**$179,449**

In response to the Board's previous decision on this matter (EB-2007-0753), Norfolk has provided an analysis of the historic spending on storm damage. Norfolk tracks storm damage repair costs in a separate maintenance sub-account.

The annual storm damage summary is as follows:

	2003	**2004**	**2005**	**2006**	**2007**
Non-Extraordinary Storm Damage	$54,607	$32,368	$54,667	$97,012	$81,303
Extraordinary Storm Damage					$164,235
Total Storm Damage	**$54,607**	**$32,368**	**$54,667**	**$97,012**	**$245,538**

In response to a Board staff interrogatory #17, Norfolk intends to expense all costs related to the Z-factor event.

Submission

Board staff notes that the 3rd Generation IRM report stated that distributors are expected to report promptly and apply to the Board for any amounts claimed under Z-factor treatment with the next rate application. Board staff notes that Norfolk did not apply for Z-factor recovery in their 2009 IRM3 application.

In response to Board staff interrogatory #15, Norfolk stated that no direction was given in the Board's Decision (EB-2007-0753) as to the timing required for the submission of future application. As well, Norfolk stated that given the short time frame between the date it received its 2008 final rate order (August 22, 2008) and its submission of its 2009 IRM application (November 7, 2008), Norfolk did not have sufficient time to adequately address the z-factor issue.

Based on its review of the evidence, Board staff notes that Norfolk has been responsive to the Board's findings in its EB-2007-0753 Decision, and the criteria of materiality, prudence and causation were met. As such, Boars staff takes no issue with the amount requested for disposition with the exception of the carrying charges being claimed. Board staff suggests that given the time elapsed between the event and this application, the Board may wish to reduce the level of carrying charges to the level that would apply had Norfolk included this claim in its 2009 IRM application. Board staff also notes that Norfolk's request to dispose of the balance over one year based on a volumetric rate rider is consistent with the EDDVAR Report.

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.

Norfolk Specific Background

Annual Disposition

Norfolk has requested the disposition of its Group 1 account balance. On January 8, 2010 Norfolk filed a submission for Deferral Variance disposition and noted that "in the original submission NPDI was in the process of reconstructing its deferral and variance accounts for the period Jan 01 2005 to Dec 31 2008, due to a number of inconsistencies found. As a place holder the account balances as available at that time were submitted with the application. At this time the reconstruction of the accounts has been completed and a new Deferral and Variance Account Workform is submitted. The account balances are materially different than those previously recorded and NPDI has adjusted its accounting records to reflect these changes. Also, updated quarterly RRR filings have been submitted for the time period involved." Board staff interrogatory #5a requested that Norfolk complete and submit an updated version 4 of the Deferral Variance Account Workform. Norfolk has complied with this request.

Global Adjustment

In response to Board staff interrogatory # 1a, Norfolk stated it had reviewed the Regulatory Audit & Accounting Bulletin 200901 and confirmed that it had accounted for its Account 1588RSVApower and global adjustment sub-account in accordance with this Bulletin. In response to Board staff interrogatory #1b, Norfolk confirmed that it had made adjustments 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, Norfolk agreed that a separate rate rider be prospectively applied to non-RPP customers to dispose of the global adjustment sub-account balance on the basis that it "would be fair to all customers". In response to Board staff interrogatory #2b, Norfolk stated that it could have the billing capability for a separate rate rider applicable to non-RPP customers to dispose of the global adjustment sub-account balance with "minor customization".

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 #4d, Norfolk "believes it should be applied to all non-RPP customers whether in the MUSH sector or not. NPDI's billing system has the ability to identify all current non-RPP customers based on pricing flags, but does not currently have the ability to identify specific customers within the MUSH sector."

Norfolk 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 $2,294,987. The balance in the 1588 global adjustment sub-account is a debit of $848,347. Norfolk 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.

Norfolk 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. However, Norfolk selected a 4-year disposition period in its Deferral Variance Account Workform V4.

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 Norfolk's RRR filings. Board staff has reviewed the balances and notes that the changes result in material differences. Norfolk response to Board staff interrogatory #5c states that it has updated and re-filed its RRR reporting and balanced the Deferral Variance disposition request to the refilled RRR balances. Board staff notes that Norfolk stated in response to staff's interrogatory # 5d that Norfolk 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.

Were the Board to have any concerns about these adjustments, Board staff proposes that the Board might consider declaring the rate riders interim until the re-filed balances can be brought forward in a future application and supported by a third party audit.

POTENTIAL LOST REVENUE ADJUSTMENT MECHANISM ("LRAM") AND SHARED SAVINGS MECHANISM ("SSM") RATE RIDER(S)

Background

Norfolk initial application requested the recovery of LRAM and SSM of $ 210,957 ($158,995 for LRAM, $ 9,600 carrying charges and $42,362 for SSM) over a one year period. The third-party review of the LRAM and SSM calculations is provided at Exhibit 1, Appendix 4 of the manager's summary.

On January 10, 2010 Norfolk submitted an update request seeking the recovery of LRAM and SSM of $269,323 ($175,997 for LRAM, $10,215 carrying charges and $83,111 for SSM) over a one year period. Norfolk's explanation for the updated amounts was that "On November 10 2009, an update from the OPA regarding NPDI's Conservation Program Results results was received. Also corrections were made to the SSM amounts as a result of necessary changes to correct mistakes noted in the Interrogatory Response process."

Submission

The Board's Guidelines for Electricity Distributor Conservation and Demand Management (the "Guidelines") issued on March 28, 2008 outlines the information that is required when filing an application for LRAM or SSM.

Based on Board Staff's review of the pre-filed evidence and interrogatory responses, it appears that Norfolk has increased its total requested LRAM and SSM amount by approximately $58,336 or 27.6%. The increase is primarily a result of having Enerspectrum recalculates the TRC, LRAM and SSM for the Energy Audits for Major Customers. The recalculation was due to turnover at the utility and the loss of the original substantiation sheets.

Board staff notes that the recalculation of the data was done by a qualified third party evaluator. Board Staff submits that although the utility did provide recalculated TRC, LRAM and SSM figures for the Energy Audits of Major Customer programs, very minimal discussion around the variances to the originally filed figures was provided. Board Staff understands that this may not have been possible due to the turnover in staff at the utility, however, without further explanation as to why the claim has increased by a material amount, Board Staff submits that the Board should not accept Norfolk's claim at this time.

ADJUSTMENTS TO THE REVENUE TO COST RATIOS

Background

The Board's Decision (EB-2007-0753) for Norfolk's 2008 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 Norfolk 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 Norfolk has complied with the filing requirements of the 2010 Supplemental Filing Module. Board staff takes no issue with Norfolk'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.

Norfolk Specific Background

Norfolk 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 Norfolk, 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 by the applicant and submits that the proposal by Norfolk 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.

Norfolk Specific Background

In response to Board staff interrogatory # 8a which asked if Norfolk agrees that a deferral account should be established to capture the reductions in OM&A and capital expenditures, Norfolk stated "NPDI will agree to treat the Harmonized Sales Tax in any manner directed to by the Board." However Norfolk submitted various reasons why it believes "any savings from a move to harmonize sales taxes should not be captured in 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 Norfolk 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 Norfolk'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 Norfolk's next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

Norfolk 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