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BY EMAIL

February 5, 2010

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

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Board Staff Submission on Hydro Ottawa Ltd.
2010 Electricity Distribution Rates Application
Board File Number EB-2009-0231

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

Hydro Ottawa Ltd. reply to submissions is due February 26, 2010.

Yours truly,

Original Signed by

Martin Benum
Advisor, Applications and Regulatory Audit

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2010 ELECTRICITY DISTRIBUTION RATES

Hydro Ottawa Ltd.

EB-2009-0231

February 5, 2010

Board Staff Submission
Hydro Ottawa Ltd.
2010 IRM3 Rate Application
EB-2009-0231

Introduction

Hydro Ottawa Ltd. ("Hydro Ottawa") 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 Hydro Ottawa 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 Hydro Ottawa.

Board staff makes submissions on the following matters:

- Tax Sharing Rate Rider – December 31, 2010 Sunset Date;
- 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") rate rider;
- Adjustments to the Retail Transmission Service Rates; and
- Accounting for the implementation of the Harmonized Sales Tax ("HST").

TAX SHARING RATE RIDER – DECEMBER 31, 2010 SUNSET DATE

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.

Hydro Ottawa Specific Background

Hydro Ottawa is proposing that the rate rider only be in effect for 8 months (May 2010 to December 2010) in order to facilitate the transition to a new rate year starting January 1, 2011. Therefore, the total tax savings to be shared was calculated outside the model, using the applicable 8 months of billing data from the approved 2008 EDR Application.

Submission

Hydro Ottawa is proposing to apply the tax savings rate rider over eight months versus an annual twelve month period. Board staff observes that this would accelerate the reduction in rates but would not change the total amount being returned to ratepayers. Board staff notes that rate riders are usually set on an annualized basis in order to minimize intra-class subsidization. However, considering the level of taxes being shared (e.g. a credit of $740,628), Board staff has no issue per se with the use of an eight month period to refund the tax savings.

Board staff further notes that this does not constitute acceptance of the notion of aligning the rate year with the fiscal year.

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.

Hydro Ottawa Specific Background

Annual Disposition

Hydro Ottawa has not requested the dispostion of its Group 1 account balance. Hydro Ottawa stated that the preset disposition threshold set by the Board was not exceeded and therefore is not seeking the disposition of its Group 1 account balance at this time.

Board staff interrogatory # 5a requested that Hydro Ottawa complete and submit an updated version 4 of the Deferral Variance Account Workform. Hydro Ottawa has complied with this request.

Global Adjustment

In response to Board staff interrogatory # 1a Hydro Ottawa 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, Hydro Ottawa confirmed that it had not 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.

Submission

Board staff submits that Hydro Ottawa 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.

POTENTIAL LOST REVENUE ADJUSTMENT MECHANISM (“LRAM”) RATE RIDER

Background

Hydro Ottawa is requesting the recovery of LRAM of $235,563 over an 8 month period. The third-party review of the LRAM calculations were prepared by third parties for the Ontario Power Authority and provided in the following reports:

- Final Evaluation Report: 2007 Summer Savings Program, Navigant Consulting, August 20, 2008;
- Final Evaluation Report: 2007 Every Kilowatt Counts Program, Navigant Consulting, June 17, 2008;
- Final Report, Impact and Process Evaluation of Ontario Power Authority’s Great Refrigerator Roundup Program, Quantec, LLC and SeeLine Group Inc., July 2, 2008;
- Support Appendices for Impact and Process Evaluation of Ontario Power Authority’s Great Refrigerator Roundup Program, Quantec, LLC and SeeLine Group Inc., July 2, 2008; and
- 2007 Great Refrigerator Roundup Evaluation Workbook.

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.

Board staff submits that Hydro Ottawa's application for LRAM recovery is consistent with the Board's Guidelines and the Board's Decision on Horizon's application (EB-2009-0192) for LRAM and SSM recovery.

With respect to Hydro Ottawa's proposal to recover the LRAM amount over 8 months, Board staff notes that rate riders are usually set on an annualized basis in order to minimize intra-class subsidization. However, considering that the amount to be recovered is not material, Board staff has no issue per se with the use of an eight month period to recover the LRAM amount. Board staff further notes that this does not constitute acceptance of the notion of aligning the rate year with the fiscal year.

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.

Hydro Ottawa Specific Background

Hydro Ottawa 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 Hydro Ottawa, included 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 Hydro Ottawa 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.

Hydro Ottawa Specific Background

In response to Board staff interrogatory # 7a which asked if Hydro Ottawa agreed that a deferral account should be established to capture the reductions in OM&A and capital expenditures, Hydro Ottawa stated that:

> "In general, Hydro Ottawa supports the use of deferral accounts to protect customers and distributors in instances such as tax rate changes. The impacts of many tax rate changes (income tax for example) can be readily identified. However, Hydro Ottawa does not agree with the Board's proposal to capture the reductions in OM&A and capital expenditures resulting from the introduction of the HST in a variance account, specifically as part of an Incentive Regulation Mechanism ("IRM") application.
>
> One of the principles of rate making under an IRM regime is that rates are decoupled from the distributor's expenses and the revenue requirement is not adjusted for any changes such as the Cost of Capital or an increase or decrease in expenses. Similarly, the changes in a distributor's costs due to the HST should not result in a change in rates and should not be captured in a variance account. There is no reason why this change should be treated any differently than the recently revised Return on Equity, or increases in property taxes that distributor must absorb."

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 Hydro Ottawa 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 Hydro Ottawa'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 Hydro Ottawa's next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

Hydro Ottawa 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