February 16, 2010

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

**Attention: Ms. Kirsten Walli, Board Secretary**

**Re: Niagara Peninsula Energy Inc. (ED-2007-0749)**
**Application to Ontario Energy Board for 2010 Distribution Rate Adjustment**
**EB-2009-0205 (Niagara Falls), EB-2009-0206 (Peninsula West)**

Dear Ms. Walli:

Please find the enclosed hard copies of Niagara Peninsula Energy's reply to Board Staff submissions, relating to our 2010 IRM rate application.

Please note that we have also submitted this file electronically via the RESS.

If you should have any questions regarding the enclosed, please feel free to contact our offices.

Sincerely,

Suzanne Wilson,
VP Finance

Attach.
SW/pb

.cc Margaret Battista, VP Customer Service & IT
Frances Conidi, Controller
Paul Blythin, Financial and Regulatory Analyst

**IN THE MATTER OF** the *Ontario Energy Board Act, 1998*, being Schedule B to the *Energy Competition Act, 1998*, S.O. 1998, c.15;

**AND IN THE MATTER OF** an Application by Niagara Peninsula Energy Inc. for an Order or Orders approving or fixing a proposed schedule of adjusted distribution rates and other charges, effective May 1, 2010.

# Niagara Peninsula Energy's Reply

# to Board Staff Submissions

**February 16, 2010.**

**Introduction**

Niagara Peninsula Energy Inc. ("NPEI") is a licensed distributor of electricity providing service to consumers within its two licensed service areas – Niagara Falls and Peninsula West. NPEI filed two applications with the Ontario Energy Board (the "Board"), on October 20, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that NPEI charges for electricity distribution, to be effective May 1, 2010. The application is based on the 2010 2nd Generation Incentive Regulation Mechanism ("IRM").

On December 10, 2009, NPEI received interrogatories on its IRM application from Ontario Energy Board Staff ("Staff"). Interrogatory responses were filed by NPEI on December 30, 2009.

On February 1, 2010, Staff made submissions on three elements of NPEI's application:

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

NPEI's replies to Staff submissions on these three matters follows below.

## Disposition of Deferral and Variance Accounts as per the EDVAR Report

### Staff Submissions

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. This rider would apply prospectively to non-RPP customers, and would exclude the MUSH sector (Municipalities, Universities, Schools and Hospitals) and other designated customers that were on RPP. As an alternative, Staff indicates that the Board may wish to consider recovering the allocated global adjustment sub-account balance from all customers in each class. This alternative approach would recognize potential customer migration between RPP and non-RPP.

Staff submits that the Board should consider approving NPEI's proposed deferral and variance account balance disposition rate riders on a final basis.

Staff proposes that the disposition period for all Group 1 accounts should not exceed one year, in order to reduce inter-generational inequities.

### Reply

NPEI agrees with Staff's submissions on this issue, with the exception of the suggested disposition period. NPEI is requesting that the deferral and variance account balances be disposed of over two years.

In its responses to Staff interrogatories, NPEI proposed several reasons why a two year disposition period would be preferred. NPEI is applying to dispose of a combined credit balance in the Group 1 accounts of almost $8 million, which represents a substantial percentage of NPEI's annual distribution revenue. NPEI believes that adopting the default disposition period of one year may induce potential strains on cash flows, due to significant expenditures on smart meters to be incurred in 2010, and increasing accounts receivable balances and bad debt expenses.

In addition, NPEI has identified that there may be some concern with customer bill impacts that would arise if a one year period were implemented: customers would receive larger credit rate riders for one year, which would then terminate at April 30, 2011. NPEI plans to file a Cost of Service rate application for rates to be effective May 1, 2011. Therefore, any potential bill impacts that would result from the implementation of the 2011 rates may be increased by the coincident timing of the credit rate riders terminating. NPEI notes that it is not necessarily desirable for customers to experience a sizeable drop in rates one year, to be followed the next year by a large increase, and submits that a two year disposition period is an acceptable approach to keeping rates more stable.

In its submission, Board Staff proposes that there would be a benefit to disposing of the account balances over one year, as this would minimize inter-generational inequities. Staff also notes that these balances have been accumulating over the last four years, and to delay immediate action is not in the best interest of the customers.

NPEI is mindful of the need to minimize inter-generational inequities, and wishes to return credit balances to its customers as soon as possible. NPEI submits, however, that the need for a timely disposition must be weighed against the concerns about cash flow and potential bill impacts. In NPEI's submission, a two year rate rider will be in the best interest of the customers, as it strikes the correct balance between these various concerns.

The EDVAR Report states: "The Board also agrees the default disposition period used to clear the Account balances through a rate rider should be one year. However, a distributor could propose a different disposition period to mitigate rate impacts or address any other applicable considerations, where appropriate." NPEI is proposing a different disposition period, both to mitigate rate impacts and address other considerations, in this case being possible cash flow strains.

NPEI would also direct the Board to its recent decision on an application by Enersource Hydro Mississauga Inc. ("Enersource") for approval to dispose of its Group 1 balances (EB-2009-0405). In its decision, the Board approved a two year disposition period for Enersource. This application involved the disposition of a net debit balance in the Group 1 accounts, as opposed to NPEI's net credit balance. However, the situation is similar to NPEI's in that Enersource's RPP customers will be billed a credit rate rider only, and the global adjustment debit balance is being recovered through a charge to non-RPP customers only.

For the reasons outlined above, NPEI encourages the Board to consider approving a two year disposition period.

## Adjustments to Retail Transmission Service Rates

### Staff submissions

NPEI has applied for adjustments to its retail transmission service rates ("RTSR") based on the July 22, 2009 RTSR Guideline proxy rate adjustment. Staff submits that the revisions to the RTSRs ought to reflect the changes from the current level to the January 1, 2010 level of Uniform Transmission Rates. This would result in increases for NPEI of 15.6% to RTSR Network Service and 5.2% to RTSR Line and Transformation Connection Service.

### Reply

NPEI accepts Staff's submissions on the adjustments to retail transmission service rates.

## Accounting for the Implementation of the Harmonized Sales Tax

### Staff Submission

Staff submits that the Board may wish to consider establishing a deferral account to record the amounts, after July 1, 2010 and until NPEI'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 NPEI's next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

NPEI 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.

### Reply

NPEI's response to Board Staff interrogatory #9A stated "NPEI proposes that the provincial related portion of the harmonized tax be captured in two accounts similar to the GST ITC account; one account for OM&A related tax and the other account for tax on capital expenditures. All debits recorded in these accounts technically would equal the reductions to OM&A and capital that are due to the harmonized tax. Reporting to the OEB on the amounts of the reductions would be based on these two accounts, which are the same accounts that would be used in preparing the monthly HST filings."

To clarify, the response was intended to convey what NPEI understands to be a necessary first step in establishing the deferral accounts proposed by Board Staff. That is, recording the amounts that were formerly incorporated as PST, and capitalized or expensed, but are now part of a harmonized tax, into separate ITC accounts. NPEI would seek further guidance from the Board on how the amounts so recorded would be used to calculate the actual balances that would be included in the deferral accounts to eventually be credited back to customers.

To elaborate, it is clear that distributors do not recover a dollar in rates for every dollar of capital expenditure or OM&A expense that will be avoided by the implementation of HST. To accurately compute the amounts related to the former

PST that are embedded in current rates, NPEI believes that it may be necessary for distributors to perform a full revenue requirement type of calculation on the amounts of the input tax credits that relate to PST, based on the parameters from their last cost of service rate application, and then apply the cumulative effect of the IRM adjustments that have been approved in the intervening years, in order to determine the amounts that are being recovered in current rates for the former PST.

Further, many purchased items that will be subject to HST are initially placed into inventory, and it is not known at the time of purchase whether the item will eventually be capitalized or expensed. Tracking the split between the HST that relates to capital and the HST that relates to OM&A for items issued from inventory will add an additional layer of complexity to the accounting process and subsequent reconciliations. In addition, there may be further complications dealing with opening inventory balances that currently contain PST versus inventory purchased after July 1, for example valuation and inventory transfers.

As noted by Staff, this treatment should only apply to subject items that are included in the category of distribution revenue requirement. In NPEI's case, as with other distributors filing 2010 2nd Generation IRM applications, the current Board-approved rate base relates back to the 2006 EDR application, and so it may not be a straightforward matter to determine which 2010 expenditures are, in fact, included in approved revenue requirement.

NPEI submits that, should the Board proceed with establishing deferral accounts to capture the amounts that are recovered in rates relating to the former PST, more specific guidelines ought to be developed to assist distributors in accurately computing the balances to be recorded in these deferral accounts. NPEI suggests that this may best be accomplished by several OEB-initiated training sessions available to all affected distributors: one for the identification of relevant issues that LDCs will encounter in attempting to implement the deferral and variance accounts suggested by Staff, and a second session that provides training on accounting for the HST. NPEI requests that further guidance and training on this matter be initiated in advance of the legislation being enacted.

All of which is respectfully submitted.