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February 19, 2010

Delivered by E-mail and Courier

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, Ontario
M4P 1E4

Dear Ms. Walli:

Re: Cambridge and North Dumfries Hydro Inc. – 2010 Cost of Service Electricity Distribution Rate Application – Board File No. EB-2009-0260

We are counsel to Cambridge and North Dumfries Hydro Inc. ("CND") in the above captioned matter.

Please find accompanying this letter CND's Argument-in-Chief in this proceeding.

Should you have any questions or require further information, please do not hesitate to contact me.

Yours very truly,
BORDEN LADNER GERVAIS LLP

Original Signed by James C. Sidlofsky

James C. Sidlofsky
JCS

cc. Theodore Antonopoulos, Ontario Energy Board
Keith Ritchie, Ontario Energy Board
John Grotheer, Cambridge and North Dumfries Hydro Inc.
Intervenors of Record

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Vancouver • Toronto • Ottawa • Montréal • Calgary

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

AND IN THE MATTER OF an application by Cambridge and North Dumfries Hydro Inc. for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2010.

CAMBRIDGE AND NORTH DUMFRIES HYDRO INC.

ARGUMENT-IN-CHIEF ON UNSETTLED MATTERS

DELIVERED FEBRUARY 19, 2010

INTRODUCTION:

1. Cambridge and North Dumfries Hydro Inc. ("CND") owns and operates the electricity distribution system in its licensed service area in the City of Cambridge and the Township of North Dumfries. CND serves approximately 50,000 Residential, General Service, Large User, Street Light and Unmetered Scattered Load customers and connections. CND also provides Low Voltage facilities to Hydro One Networks Inc. and Waterloo North Hydro Inc.

2. CND filed an application (the "Application") with the Ontario Energy Board (the "Board") on August 31, 2009 under section 78 of the *Ontario Energy Board Act*, *1998*, S.O. 1998, c. 15, (Schedule B), seeking approval for changes to the rates that CND charges for electricity distribution, to be effective May 1, 2010. The Board assigned the File Number EB-2009-0260 to the Application. Three parties requested and were granted intervenor status: Energy Probe ("EP"), the School Energy Coalition ("Schools"), and the Vulnerable Energy Consumers Coalition ("VECC").

3. The Board issued Procedural Order No. 1 on October 23, 2009. Board staff filed interrogatories on November 5, 2009, and all registered intervenors filed interrogatories by November 9, 2009. CND filed responses to interrogatories on November 30, 2009. The Board issued Procedural Order No. 2 on December 14, 2009. That Procedural Order provided for supplemental interrogatories and a

Settlement Conference. CND responded to supplemental interrogatories from Board staff and certain of the intervenors on January 13, 2010. The evidence in this proceeding (referred to herein as the "Evidence") consists of the Application and CND's responses to both the initial and supplemental rounds of interrogatories.

4. The Settlement Conference was conducted on January 20, 2010, at the Board's offices, with Kenneth Rosenberg acting as facilitator. Representatives of the Applicant and intervenors (Energy Probe, the School Energy Coalition and the Vulnerable Energy Consumers Coalition) participated in the Settlement Conference, and Board staff participated in accordance with their role as set out in the Board's Settlement Conference Guidelines.

5. The parties achieved a partial settlement in this proceeding. A Settlement Agreement was filed on February 10, 2010, with an updated version reflecting a reduction in the PILs calculation filed on February 17, 2010. By a Decision dated February 18, 2010, the Board approved the Settlement Agreement.

6. In the Settlement Agreement, the parties set out the unsettled matters and proposed that they would be the subject of written submissions. CND has reproduced the descriptions of those issues from the Settlement Agreement below, for the Board's assistance:

Rate Base:

- the appropriate treatment of Ontario's shift to a Harmonized Sales Tax, planned for implementation effective July 1, 2010, with respect to both capital expenditures and Operating Costs; and
- the appropriateness of a lead-lag study being required for CND's next cost of service application.

Operating Revenue:

- the appropriateness of CND's load forecast, including the impact of CDM initiatives, for the 2010 Test Year.

- The appropriate treatment for rate making purposes of CND's forecast reduction in a shared services-related revenue offset of $440,000 – the offset will be reduced to $330,000 in the 2010 Test Year and to $0 in each year of the IRM period as CND will no longer be providing those services.

Operating Costs:

- The Parties agree that CND will incur an OM&A expenditure in the 2010 Test Year in the amount of $42,500 related to CND's change to monthly billing as part of the implementation of its new CIS system in November 2010. The Parties agree that CND's annual costs related to this change during the IRM period will be $312,000. The submissions will address the question of whether the appropriate amount for inclusion in CND's 2010 Revenue Requirement should be $42,500 or a "normalized" value of the 2010-2013 expenditure of $244,625 (representing $42,500 for 2010 plus three years at $312,000).

Cost of Capital and Capital Structure:

- The percentage of CND's regulated capital structure that should be made up of short-term debt.

- The appropriate allowed Return on Equity.

Deferral and Variance Accounts:

- Board Staff have inquired as to whether CND's billing system is capable of assigning the balance in the Account 1588 RSVA Power Account – Global Adjustment Sub-Account only to non-RPP customers. The Parties take no position in this regard, although CND notes that its billing system is not capable of creating distinctions among members of the same class with respect to rate riders. The parties mention this matter in order to ensure that Board staff will have an opportunity to comment on it in the submissions that will follow the Board's approval of this Settlement Agreement. However, this should be considered a severable issue, in that the Board's determination of this matter will not affect the settlement among the Parties.

SUBMISSIONS ON THE UNSETTLED MATTERS:

7. CND offers its submissions on these matters below. CND will have further comments on these matters in its reply argument, following receipt of the Board staff and intervenor submissions.

Rate Base:

- **the appropriate treatment of Ontario's shift to a Harmonized Sales Tax, planned for implementation effective July 1, 2010, with respect to both capital expenditures and Operating Costs**

8. In accordance with its response to Board staff Supplemental Interrogatory #42, CND believes that this is an industry-wide issue that should be addressed consistently for all distributors across the sector. CND suggests that this requires a decision from the Board that could be the result of a public consultation process whereby all of the viable alternatives are discussed.

9. In the event that the Board directs all electricity distributors to capture the reductions in OM&A and capital expenditures resulting from the change to HST in variance accounts, CND would follow the Board's direction and record all incremental reductions.

10. CND notes, however, that the recording of differences stemming from PST and GST harmonization would require a substantial effort on the part of CND and administrative costs would increase significantly due to the following factors:

- Sales taxes are recorded in CND's financial system at the invoice level so sales taxes paid are easily identifiable at the vendor invoice level; however, inventory consumptions will often be split among capital, OM&A and third party billings. CND would not be able to track "PST and GST harmonization" variances without tracking each single individual line item from every invoice where harmonized taxes were paid. The ultimate tracking of inventory items would be very complex.

- Recording variances would require a higher level of technical knowledge at the Accounts Payable entry point than is currently the case. The Accounts Payable clerk capturing this data would have to have technical expertise on the application of both PST and GST rules (old and new), in order to deal with (for example) expenses that were previously PST exempt but will be subject to the full HST under the new rule. This monitoring requires more skilled accounting personnel and labour intensive supervision on the AP process.

- There are also complicated transition rules that apply to businesses with greater than $10 million in sales, and that will increase labour and supervisory costs to ensure proper accounting treatment.

11. Additionally, the cost impact on CND of the switch from PST to HST is unknown at this time and may never be accurately determined. The cost impact will consist of the (effective) removal of an 8% tax component on both capital goods and other operating supplies and services, offset by the fact that depending on market conditions for each of these goods and services, prices will increase as suppliers fail to pass through the full tax reduction in prices. Information on the degree to which prices fail to reflect the full tax change will necessarily be speculative and in all probability could not form the basis for accounting entries. Therefore, CND does not accept the suggestion that accurate entries could be made in such a deferral account if it were established.

12. An alternative with respect to OM&A would be a reduction in the monthly fixed charges for all customers in all utilities (i.e. rate rebasing and IRM) effective May 1, 2010. The amount could be $0.10 per month per customer to reflect the implementation date of July 1, 2010 for HST impacts. However, CND again stresses that any such approach should be the result of a sector-wide consultation, and not imposed on an application-by-application basis.

13. With respect to capital expenditures, CND considers the impact of the change to not be material. This is because the amortization periods spread any savings that

might exist over long time periods and the rebasing process will capture the changes in a timely manner.

- **The appropriateness of a lead-lag study being required for CND's next cost of service application.**

14. In accordance with its response to VECC Interrogatory #11(d), CND notes that according to Chapter 2 of the Filing Requirements for Transmission and Distribution Applications issued by the Board on May 27, 2009, in section 2.3.4, the Board provides applicants with two approaches to calculate their allowance for working capital: (1) the 15% allowance approach, or (2) filing a lead-lag study. CND selected the first option.

15. CND understands that for distributors that were a similar size to CND and that rebased in 2009 through cost of service applications, the Board did not require those distributors to complete a lead-lag study as a result of the significant cost of the study. CND did not believe it would be cost effective to conduct such a study for this application, nor does it believe that such a study would be cost-effective for its next cost of service application.

Operating Revenue:

- **the appropriateness of CND's load forecast, including the impact of CDM initiatives, for the 2010 Test Year.**

16. In the course of the interrogatory process, CND revised its purchased load forecast downward from 1,522,594 MWh as shown in the Application, to 1,420,552 MWh. The reduction stems from VECC Interrogatories 14(c) and (f), and CND's responses to them. The response to Interrogatory 14(c) led to a reduction to 1,429,225 MWh, and the response to Interrogatory 14(f) led to the balance of the reduction to 1,420,552 MWh.

17. In response to VECC 14(c), which addressed the issue of a counterintuitive negative coefficient on the population variable used in the load forecast and the

direct impacts of CDM, CND reran the regression analysis and included a trend variable, as requested by VECC, to capture CDM. The trend variable starts at 1 on January 2006 and grows to 60 by December 2010. The following table provides the resulting statistics and a forecast for 2009 and 2010:

Regression Statistics	Value
Multiple R	97.8%
R Square	95.7%
Adjusted R Square	95.4%
F- Test	407.4
T-Stats by Coefficient	
Intercept	(6.90)
Heating Degree Days	12.91
Cooling Degree Days	5.74
Ontario Real GDP Monthly	4.07
Number of Days in Month	7.47
Spring Fall Flag	0.13
Population	2.01
Number of Peak Hours	8.78
CDM Flag	(6.83)
Purchased Forecast	
2009 (W N) - kWh	1,468,651,648
2010 (W N) - kWh	1,429,225,393

18. In response to VECC's request in Interrogatory #14(f), CND then updated the Ontario GDP numbers assumed in the 2009 and 2010 forecast to reflect the Ontario GDP information provided on October 22, 2009 by the Ontario Minister of Finance in the fall update to the 2009 Ontario Economic Outlook and Fiscal Review. In this fall update, the 2009 GDP was updated from -2.5% to -3.5% and the 2010 GDP was updated from 2.3% to 2.0%.

19. CND submits that the revised forecast of 1,420,552 MWh provides a superior forecast to the one provided in the application as this forecast:

a) addresses the issue raised by Board staff and Intervenors with respect to the counterintuitive negative coefficient on the population variable used in the load forecast;

b) provides a better Rsquare value or "fit" of forecast to actual data of 95.7% compared to the Rsquare value of 94.3% for the forecast used in the Application;

c) reflects updated Ontario GDP values; and

d) is consistent with the actual 2009 purchased value of 1,450,836 MWh for CND.

- **The appropriate treatment for rate making purposes of CND's forecast reduction in a shared services-related revenue offset of $440,000 – the offset will be reduced to $330,000 in the 2010 Test Year and to $0 in each year of the IRM period as CND will no longer be providing those services.**

20. As discussed in the Settlement Agreement, CND forecasts that it will lose the sum of $110,000 in the 2010 Test Year as a result of the discontinuation of water and sewer billing services to the City of Cambridge and the Region of Waterloo as of September 30, 2010.[1] In other words, the forecast shared services-related revenue offset of $440,000 will be reduced to $330,000 in the 2010 Test Year. CND further forecasts it will have a revenue shortfall of $440,000 for each year of the IRM period as it will no longer be providing these services. The Parties have agreed that the question of whether the appropriate amount for inclusion in CND's 2010 Revenue Requirement should be the 2010 forgone revenue ($110,000 per CND's forecast) or a "normalized" value of the 2010-2013 expenditure ($357,500 - representing $110,000 for 2010 plus three years at $440,000 per CND's forecasts) will be the subject of written submissions.

[1] This was addressed in CND's responses to Schools Interrogatory #13(a) and EP Interrogatory #24(f)

21. CND submits that there is no dispute as to the accuracy of the $110,000 in lost offsets related to water and sewer billing in 2010 and the $440,000 in lost offsets for each of 2011, 2012 and 2013. There are two possible approaches to this issue – the Board could allow only the recovery of the revenue offset of $110,000 that will be forgone in the 2010 Test Year, which means that for each IRM year, CND will necessarily have a revenue shortfall of $330,000; or the Board could recognize that for each of the three IRM years that follow, CND will lose an offset of $440,000 and provide for that through an adjustment to the 2010 water and sewer billing-related offset that will carry through the 2010 IRM period.

22. CND submits that the latter approach is the appropriate and reasonable one, and it is consistent with the approach adopted by the Board in its recent (December 1, 2009) Decision in the matter of Greater Sudbury Hydro Inc.'s 2009 cost of service distribution rate application (EB-2008-0230), with respect to certain costs that would not be incurred by the utility until the year following the Test Year.

23. CND submits that generally, there is an inherent assumption when dealing with revenue offsets that the offset will continue through the IRM period. Here, this is clearly not the case. Limiting CND's recovery to the $110,000 to be lost in relation to the 2010 Test Year will mean that CND will have insufficient funds to meet its revenue requirement through the IRM period.

24. This is similar to the Greater Sudbury Hydro situation – in that case, Greater Sudbury Hydro had included a $100,000 expense in its 2009 rate application for maintenance costs related to its ERP system and WIPRO. However, those expenses would not be incurred until 2010. At page 18 of its Decision, the Board made the following findings:

> **"4 h. Enterprise Resource Planning ("ERP") Maintenance Costs**
>
> Greater Sudbury has included $100,000 for maintenance of the ERP system and WIPRO. However these costs will not be incurred until 2010. SEC submitted that these costs should not be included in OM&A.

Board Finding

The Board finds the inclusion of $100,000 in 2009 to be inappropriate. However, a total exclusion, which would not recognize the incurrence of these fees after 2009 which is during the IRM phase, would leave Greater Sudbury without the appropriate level of revenue to offset these costs. The Board finds that $75,000 a year until the next rebasing is appropriate under the circumstances."

25. The effect of that decision was that the $300,000 in expenditures that Greater Sudbury Hydro would be incurring in the three year (2010 – 2012) IRM period following the 2009 Test Year were "normalized" so that the utility would recover the $300,000 (and no more) over the four year period that included the Test Year.

26. CND submits that there should be no distinction between the treatment of an expense (the Sudbury situation) and the loss of a revenue offset (the CND case) – in both cases, the distributor will not have the appropriate level of revenue to offset its costs through the IRM period. CND submits that the Board's approach in the Greater Sudbury case is the correct approach in the current case as well – in this way, by including $357,500 in the 2010 Test Year revenue requirement, CND will recover the "appropriate level of revenue to offset its costs."

Operating Costs:

- **The Parties agree that CND will incur an OM&A expenditure in the 2010 Test Year in the amount of $42,500 related to CND's change to monthly billing as part of the implementation of its new CIS system in November 2010. The Parties agree that CND's annual costs related to this change during the IRM period will be $312,000. The submissions will address the question of whether the appropriate amount for inclusion in CND's 2010 Revenue Requirement should be $42,500 or a "normalized" value of the 2010-2013 expenditure of $244,625 (representing $42,500 for 2010 plus three years at $312,000).**

27. With respect to this matter, CND's comments are similar to those under Issue 3(e), above, and CND refers the Board to them. The change to monthly billing was discussed in Exhibit 4, at pages 32 and 33. The annual cost of $312,000 consists

of $255,000 in third party costs plus staffing increases with a value of $57,000.[2] As in the Greater Sudbury case, CND will be incurring higher costs in the IRM period than would be incorporated into the Test Year revenue requirement. In Greater Sudbury's case, none of those costs were being incurred in the Test Year; in CND's case, only a small portion of the ongoing costs are being incurred in the Test Year. Limiting CND's recovery to the $42,500 to be spent during the 2010 Test Year will mean that CND will have insufficient funds to meet its revenue requirement through the IRM period.

28. CND submits that the inclusion of $244,625 in the 2010 Test Year revenue requirement will allow for the recovery by CND of the "appropriate level of revenue to offset its costs."

Cost of Capital and Capital Structure:

- **The percentage of CND's regulated capital structure that should be made up of short-term debt.**
- **The appropriate allowed Return on Equity.**

29. The Parties agree that CND's proposed debt to equity ratio for rate making purposes of 60% to 40% is appropriate. However, the following two matters are not settled with respect to cost of capital:

   - The percentage of CND's regulated capital structure that should be made up of short-term debt. The debt component is comprised of 56% long term debt and 4% short term debt. The intervenors, do not agree that 4% short term debt is an appropriate amount for CND for rate making purposes. The Parties have agreed that this matter will be the subject of written submissions.
   - The Application was prepared using the Board's 2009 cost of capital parameters, but provides for an adjustment based on the Board's updated cost of capital parameters. CND's position is that the methodology for determining the Return on Equity for the 2010 Test Year is as set out in the December 11, 2009 *Report of the Board on the Cost of Capital for Ontario's Regulated*

[2] See CND's response to Energy Probe Interrogatory #34(d).

Utilities, and that the Return on Equity applicable to CND should be determined on that basis. The intervenors do not agree that the rate should be determined as provided for in that Report. The Parties have agreed that this matter will be the subject of written submissions.

30. CND's deemed debt capitalization includes 4% of short term and 56% of long term debt in accordance with the Board's December 20, 2006 Cost of Capital Report. CND submits that the December 11, 2009 Report of the Board on the Cost of Capital for Ontario's Regulated Utilities, the result of a lengthy review by the Board, recognized (at page 56) that "The short-term debt rate, and deemed 4% component of the capital structure was introduced in Cost of Service applications for 2008 distribution rates", and the Board did not alter the deemed debt capitalization percentages for short and long term debt. The percentages were confirmed in the December 11, 2009 report (see, for example, the summary at Section 4.5, Table 2, page 59 of the Report). Accordingly, CND submits that the short term debt percentage of rate base should be 4% and long term debt component should be 56% for 2010 rate setting purposes. CND submits that any changes to this approach, which has now been in place for several years of cost of service applications, including 2010 cost of service applications, can only come about through a sector-wide review process, and must not be the result of *ad hoc* requests in individual cost of service applications.

31. Similarly, with regard to Return on Equity, CND submits that the methodology for determining the Return on Equity for the 2010 Test Year is as set out in the December 11, 2009 *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities*, and that the Return on Equity applicable to CND should be determined on that basis, consistent with the Board's approach to other rebasing distributors. As the Board noted at page VI of that Report, based on September 2009 data, the base ROE is set at 9.75%." Once again, any changes to this approach can only come about through a sector-wide review process, and must not be the result of *ad hoc* requests in individual cost of service applications.

Deferral and Variance Accounts:

- **Board Staff have inquired as to whether CND's billing system is capable of assigning the balance in the Account 1588 RSVA Power Account – Global Adjustment Sub-Account only to non-RPP customers. The Parties take no position in this regard, although CND notes that its billing system is not capable of creating distinctions among members of the same class with respect to rate riders. The parties mention this matter in order to ensure that Board staff will have an opportunity to comment on it in the submissions that will follow the Board's approval of this Settlement Agreement. However, this should be considered a severable issue, in that the Board's determination of this matter will not affect the settlement among the Parties.**

32. For the purposes of this submission, CND confirms that its billing system is not capable of creating distinctions among members of the same class with respect to rate riders and would request that the Board take this into consideration when it renders its decision on this issue. As with all of the unsettled matters, CND may have further comments in this regard in its reply argument following receipt of the Board staff submissions.

CONCLUSION:

33. For all of the foregoing reasons, CND respectfully requests that the Board:

a) deal with the shift to HST on a consistent industry-wide basis through an appropriate consultation process;

b) not require CND to prepare a lead lag study for its next cost of service application;

c) approve CND's load forecast of 1,420,552 GWh, which incorporates revisions through its responses to VECC Interrogatories 14(c) and (f);

d) allow the inclusion of $357,500 in its 2010 Test Year revenue requirement, which recognizes the loss of $110,000 in water and sewer billing-related revenue offsets for the 2010 Test Year and $440,000 per year for each of the three IRM years that follow;

e) allow the inclusion of $244,625 in its 2010 Test Year revenue requirement, which recognizes $42,500 in CIS costs related to the shift to monthly billing for the 2010 Test Year plus costs of $312,000 per year for each of the three IRM years that follow;

f) confirm that CND's deemed debt capitalization will be 4% of short term and 56% of long term debt in accordance with the Board's December 20, 2006 Cost of Capital Report;

g) confirm that the the methodology for determining the Return on Equity for the 2010 Test Year is as set out in the December 11, 2009 *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities*, and that the Return on Equity applicable to CND will be determined on that basis; and

h) confirm that CND will not be required incur new expenses to create distinctions within its customer classes for the purpose of assigning the balance in the Account 1588 RSVA Power Account – Global Adjustment Sub-Account – only to non-RPP customers.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 19TH DAY OF FEBRUARY, 2010:

BORDEN LADNER GERVAIS LLP
Per:

Original signed by James C. Sidlofsky
James C. Sidlofsky
Counsel to Cambridge and North Dumfries Hydro Inc.

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