February 26, 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: PowerStream Reply Submission
PowerStream Distribution Inc.
Board File Number EB-2009-0246

Please find attached the PowerStream Inc. ("PowerStream") Reply Submission for the above proceeding.

Yours truly,

Original Signed by Tom Barrett

Tom Barrett
Manager, Rate Applications

REPLY SUBMISSION

2010 ELECTRICITY DISTRIBUTION RATES

PowerStream Inc.
EB-2009-0246

February 26, 2010

PowerStream Reply Submission
Powerstream Inc.
2010 IRM 3 Rate Application
EB-2009-0246

Introduction

PowerStream Inc. (“Powerstream”) filed an application with the Ontario Energy Board (the “Board”) on October 21, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that PowerStream charges for electricity distribution, to be effective May 1, 2010. The application was based on the 2010 3rd Generation Incentive Regulation Mechanism.

On February 5, 2010, Board staff made 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”);
- Treatment of Smart Meter Funding Adder;
- Adjustments to the Large User Class;
- Adjustments to the Retail Transmission Service Rates; and
- Accounting for the implementation of the Harmonized Sales Tax (“HST”).

PowerStream respectfully offers the following replies to the Board staff submissions.

DISPOSITION OF DEFERRAL AND VARIANCE ACCOUNTS AS PER THE EDDVAR REPORT

PowerStream agrees with Board staff submission.

TREATMENT OF SMART METER FUNDING ADDER

PowerStream agrees with Board staff submission.

ADJUSTMENT TO THE LARGE USER CLASS

In its submission, Board Staff states:

"Based on section 2.5.5 of the Distribution System Code, a distributor can assign a non-residential customer to a different rate class as a result of a review initiated by the distributor as long as the distributor gives the customer written notice of the reclassification no less than one billing cycle before the reclassification takes effect for billing purposes.

Board staff has reviewed PowerStream's request and agrees that the proposed adjustments to the GS>50 and Large Use rate classes are overall revenue neutral from the perspective of the distributor.

However, Board staff has several other concerns with this proposal.

First, Board staff notes that these adjustments may not be revenue neutral at the customer level. PowerStream should confirm whether or not, all else being equal, the rates of the existing Large Use customer would increase and the rates paid by the two customers currently in the GS>50 rate class would decrease. This may arise as a result of blending the revenues associated with the two GS>50 customers with the revenue of the existing Large Use customer to derive a single set of rates that would be applicable to all three customers. Board staff estimates that the impact on the existing Large Use customer would be approximately $96,000 per year or an increase of about 86% of the distribution component of the customers bill.

Second, PowerStream provided no evidence that the revenue associated with the existing GS>50 customers is representative of the costs that would have been allocated to the Large Use class were a cost of service study conducted that would reflect the characteristics of these customers. It is also unclear whether it is appropriate to include these two customers in the Large Use rate class given the specific characteristics of the existing customer currently in that class.
Third, associated with the customer re-classification is presumably an increase in load which will generate additional revenues for PowerStream under a price cap regime. Based on staff's review of the evidence, this was not taken into account.
Fourth, parties agreed in PowerStream's 2009 Settlement Agreement (EB-2008-0244) that the revenue-to-cost ratio for the Large Use class be adjusted down to 115%. There is no evidence that demonstrates compliance with this Agreement or that supports any departure from it.

Board staff submits that the Board may wish to consider denying PowerStream's request pending a full review of this matter on the basis of a lack of supporting evidence that demonstrates the reasonableness of this proposal from a cost causality standpoint, and the impact of this proposal on affected customers."

Reply Submission

PowerStream's Large Use class contains only one customer that uses a dedicated connection that is a short distance from a transformer station. Consequently, the current Large Use rates reflect the unique circumstances of this customer and may not reflect the cost of serving new customers in this class. At the time of 2010 IRM application, PowerStream considered re-classification of two GS>50 customers to the Large Use class, based on their load characteristics. Accordingly, at that time PowerStream proposed a revenue-neutral adjustment to the distribution rates to mitigate the issue and to allow the re-classification.

PowerStream is prepared to accept the Board staff submission and postpone the adjustments to Large Use distribution rates pending an updated Cost Allocation Study. PowerStream agrees that the proposed Large Use rates are the approximate rates, which may not accurately reflect the cost of serving those customers. A comprehensive Cost Allocation Study is needed for an accurate revenue-to-cost ratios analysis and consequent rate design.

PowerStream's current distribution rate for the Large Use class is customer-specific and thus does not reflect the costs of serving any future customers that could be classified as Large Use based on their load characteristics. Therefore, to ensure the fair treatment of all customers, PowerStream submits that any new or existing customers with average monthly demand of 5,000 kW or greater be treated as GS> 50 customers until such time as rates for the Large Use class are revised based on a Cost Allocation Study reflecting the change in the composition of Large Use customers.

Based on a January 2010 review of customer consumption levels, PowerStream identified a single customer that has an average demand in excess of 5,000 kW. This customer would not be reclassified to the Large User class.

ADJUSTMENT TO THE RETAIL TRANSMISSION SERVICE RATES (RTSR)

PowerStream agrees with the Board staff submission that the Uniform Transmission Rates should be updated to reflect January 1, 2010 increased costs. PowerStream updated the calculations of RTSR to reflect the January 1, 2010 UTR adjustments. The revised calculations are shown in the attached Appendix A.

ACCOUNTING FOR THE IMPLEMENTATION OF THE HARMONIZED SALES TAX ("HST")

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

<u>Reply Submission</u>

In response to Interrogatory #10, PowerStream indicated that during an incentive regulation period, it is expected that costs will fluctuate but the distributor must manage these changes in order to meet the allowed rate of return. PowerStream pointed out a number of practical concerns with respect to establishing a deferral account related to the harmonized sales tax (HST), including transitional issues, uncertainty about increased costs and increased demands on cash flow. Finally, PowerStream indicated willingness to participate in industry-wide consultation, if such an approach were to be undertaken by the Board.

In this Reply Submission, PowerStream would like to expand upon these issues under the following headings:

- Incentive Regulation
- Practical Considerations
- Generic Approach

Incentive Regulation

The underlying premise of Incentive Regulation (IR) is that during the period between rebasings, the distributor has the opportunity to manage the cost components of distribution revenue in order to meet the allowed return on equity. It is expected that during any IR period, costs categories will rise or fall and the distributor must manage the net result.

PowerStream notes that HST is a tax on consumption rather than income. The Board's Third Generation Incentive Regulation Model takes into account income tax changes, sharing these 50% with customers. This is easily administered since the changes are applied to known base amounts. Unlike income tax changes, HST will affect a number of elements within distribution rates, therefore implementing a similar model for HST within an IR period is significantly more complex, with some of the challenges noted below.

In advancing the HST issue to update recent events, but excluding other recent events, such as changes in cost of capital or load loss, Board staff contradicts the Board's position of opposing single-issue ratemaking. PowerStream notes that load loss and cost of capital would be relatively simple to address in an IRM year compared to the complexity involved in addressing PST versus HST.

Practical Considerations

The term HST is somewhat of a misnomer in that the Ontario Provincial Sales Tax (OPST) in not being harmonized with the Goods and Services Tax (GST) on July 1, 2010, but rather the OPST is being cancelled simultaneous with an increase in the GST from 5% to 13%. The higher GST is referred to as the HST, is administered by the Federal Government, and the 8% collected will flow back to the Province of Ontario. The HST is generally subject to the same rules as the GST in that commercial organizations can claim a full Input Tax Credit (ITC) for most purchases.

Although the HST framework is relatively straight-forward, there are a number of practical considerations:

- There are a number of areas (called Temporary ITC Restrictions) where an amount equivalent to the OPST cannot be claimed as part of the ITC. These restrictions directly impact distributors. This includes licensed road vehicles under 3,000kg (including parts, certain service and fuel), electricity, gas, and combustibles except where used in manufacturing, telecommunications services other than internet access and toll-free numbers and food, beverages and entertainment. The ITC restrictions are in place for five years followed by a three year phase-out. There is increased cost to track and administer these restrictions.

- It should be noted that the provincial portion of the HST paid on electricity and natural gas costs, not eligible for the HST input tax credit, represent an additional cost that did not exist before rather than a savings.
- There is no certainty that when the OPST ends June 30, 2010 that the price paid for goods previously subject to the OPST will decline. Prices can fluctuate for any number of reasons, including market forces. For example, if a piece of equipment was purchased for $100 on June 30, the total cost would be $108 once the 8% OPST was included. There would be no ITC to claim. If however, an identical item was purchased for $110 on July 1, it would be subject to HST of 13% or $14.30. This $14.30 amount could be claimed as an ITC so the net cost of the equipment would be $110, or $2 higher than previously. It would seem inappropriate to record the provincial portion of the ITC in a deferral account since there has been no saving.
- All things being equal, bad debt expense will increase 8%. Similarly, the IESO invoice will increase 8%, putting significant pressure on working capital
- Rate base will increase slower than when the OPST was in place since, except for the ITC restriction areas, the OPST will not be booked to fixed assets. At the time of the next cost of services rate review, rate base will be lower than it otherwise would have been, thus reducing potential return.

Generic Approach

PowerStream is of the view that consideration of the impact of the HST in an issue that affects all distributors. The creation of deferral account, if that is in fact appropriate, needs careful design in order to accurately capture the correct cost elements.

PowerStream submits that Board should consider the HST issue in an industry-wide, generic context and not as part of the 2010 IRM rate application.

All of which is respectfully submitted.

Appendix A

PowerStream Inc.

2010 Retail Transmission Rates Adjustment

Change in Wholesale Costs

Updated Feb 1, 2010

Table 1: January 1, 2010 Rates and Current 2009 Rates

Uniform Transmission Rates, IESO					
Type		*Prior Jan 1/10*		*Effect. Jan 1/10*	*Percent Change*
Network	$	2.66	$	2.97	11.65%
Line Connection	$	0.70	$	0.73	4.29%
Transformation	$	1.57	$	1.71	8.92%
Sub-Transmission Rates, HYDRO ONE					
Type		*Prior Jan 1/10*		*Effect. Jan 1/10*	*Percent Change*
Network	$	2.24	$	2.37	5.80%
Line Connection	$	0.60	$	0.61	1.67%
Transformation	$	1.39	$	1.37	-1.44%

Table 2: Wholesale Transmission Network Cost

	Coincident Peak		**at 2009 rates**		**at 2010 rates**		**Change $**	**%**
IESO Billings	11,658,511	$	31,011,641	$	34,625,779	$	3,614,139	11.7%
Hydro One Billings	1,953,832	$	4,376,584	$	4,630,582	$	253,998	5.8%
Total	**13,612,343**	**$**	**35,388,224**	**$**	**39,256,361**	**$**	**3,868,137**	**10.9%**

Table 3: Wholesale Transmission Connection Cost

	Coincident Peak		**at 2009 rates**		**at 2010 rates**		**Change $**	**%**
IESO Billings								
Line Connection	12,356,307	$	8,649,415	$	9,020,104	$	370,689	4.3%
Trans. Connection	1,835,116	$	2,881,132	$	3,138,049	$	256,916	8.9%
		$	11,530,547	$	12,158,153	$	627,605	5.4%
Hydro One Billings								
Line Connection	1,972,418	$	1,183,451	$	1,203,175	$	19,724	1.7%
Trans. Connection	1,972,418	$	2,741,661	$	2,702,213	$	(39,448)	-1.4%
		$	3,925,112	$	3,905,388	$	(19,724)	-0.5%
Total		**$**	**15,455,659**	**$**	**16,063,540**	**$**	**607,881**	**3.9%**