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December 16, 2007

VIA Email and Courier

Ms. Kirsten Walli
Board Secretary
P.O. Box 2319
2300 Yonge St.
Toronto, ON
M4P 1E4

Dear Ms. Walli,

Re: Hydro 2000 Inc., EB-2007-0704

Please find the final argument filed on behalf of VECC in the above noted proceeding. It is my understanding that we are one business day late in filing our argument; on behalf of VECC I apologize for the delay in filing. Amongst other reasons, I was personally unavailable in the latter part of last week due to the birth of my daughter by way of caesarean section.

Yours truly,

Michael Buonaguro
Counsel for VECC
Encl.

ONTARIO ENERGY BOARD

**IN THE MATTER OF the *Ontario Energy Board Act, 1998*,
S.O. 1998, c. 15, Sch.B, as amended;**

**AND IN THE MATTER OF an Application by Hydro 2000
Inc. pursuant to section 78 of the *Ontario Energy Board
Act* for an Order or Orders approving just and
reasonable rates for the delivery and distribution of
electricity.**

**FINAL SUBMISSIONS
On Behalf of
VULNERABLE ENERGY CONSUMERS COALITION (VECC)**

December 16, 2007

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Vulnerable Energy Consumers' Coalition (VECC) Final Argument

The Application

On September 13, 2007 Hydro 2000 submitted an Application to the Ontario Energy Board for approval of its proposed 2008 distribution rates. This application was based on a projected 2008 Distribution revenue requirement of \$563,064 which, after an allowance for \$35,980 revenue from other sources, left \$527,084 to be recovered through distribution rates. Included in this distribution revenue requirement was \$121,000 in LV charges (from Hydro One Networks) and the impacts of planned capital spending by Hydro 2000 on Smart Meters. Also included in the Application was a request to clear the balances in a number of deferral and variance accounts and to create a new deferral account to capture capital expenses in future years 2009 and 2010.

On November 19, 2007, Hydro 2000 submitted responses to interrogatories from interested parties and also updated its Application. The revised Application included a projected 2008 Distribution revenue requirement of \$500,727 which, after the allowance for other revenue, left \$464,747 to be recover from distribution rates. Included in this requirement is an updated value for LV charges (\$143,000) and the revenue impact of the Board's currently approved Smart Meter adder of \$0.26/meter/month (\$3,594)¹.

Distribution revenues at current rates would produce revenues of \$361,518.40² which results in a deficiency of \$102,494.30 (including LV charges and provision for smart meters). This yields a required increase in distribution rates of 28.3%.

Rate Base and Capital Spending

Additions to fixed plant over the 2006-2008 period are as follows³:

- 2006 \$51,362 (net of \$64,783 in capital contributions)
- 2007 \$36,798 (net of \$42,382 in capital contributions)
- 2008 \$97,200

The large increase in 2008 is due to \$57,200 of spending to convert Hydro 2000's billing system as a result of the existing system no longer being supported. The choice of Harris was the result of an RFP process⁴.

¹ Updated Application, Exhibit 1, Tab 2, Schedule 4

² Updated Application, Exhibit 7, Tab 1, Schedule 1

³ Updated Application, Exhibit2, Tab 2, Schedule 1, page 16

⁴ See Response to OEB Staff #1 b)

VECC has no submissions or issues regarding Hydro 2000's proposed capital spending.

The overall rate base for Hydro 2000 increases from an actual value of \$698,009 in 2006 to \$735,075 in 2008. The net fixed asset portion of the rate base increases by 5%; while the allowance for working capital increases by 5.6%. With respect to the calculation of allowance for working capital, Hydro 2000 has chosen to calculate the allowance based on 15% of O&A plus Cost of Power. VECC's submissions regarding O&A expense are set out in a subsequent section.

With respect to the Cost of Power estimate used, Hydro 2000 has not provided any explanation as to the basis for the value attributed to Power Purchased (\$1,601,226) which is 6.7% higher than actual costs for 2006. However, the value appears reasonable given the forecast increase in load and likely changes in market prices. On the other hand, VECC does not understand the 7% increase in Transmission Connection charge that Hydro 2000 is forecasting for 2008 over 2007⁵. Indeed, VECC submits this value should only be increased with Hydro 2000's load growth unless Hydro One Networks (Distribution) adjusts its Transmission service charges as a result of the Board's EB-2007-0759 Decision regarding Uniform Transmission Rates effective November 1, 2007; even in such event, the costs could go down. Accordingly VECC would ask that Hydro 2000 clarify its assumptions regarding the Cost of Power component of the Allowance for Working Capital Calculation as part of its Reply Submissions.

Load Forecast and Revenue Offsets

Hydro 2000 has used the 2004 weather normalized load data developed by Hydro One Networks to establish weather normalized use per customer for each customer class. It has then developed its load forecast by forecasting 2008 customer count (by class) and multiplying this "count" by the weather normalized per customer use for each class. However, Hydro 2000 has noted some concerns regarding the methodology⁶.

Having reviewed the revised Application and the interrogatory responses, there appear to be some continuing inconsistencies in the data presented:

- it is unclear to VECC whether the normalized average consumption (NAC) presented for each rate class⁷ is based on customer class loads as measured at point of delivery to the customer or as measured at point delivery to Hydro 2000 (and therefore inclusive of losses). The text preceding the Table with the factors would suggest that they are

⁵ Updated Application, Exhibit 2, Tab 4, Schedule 1, page 5

⁶ Updated Application, Exhibit 3, Tab 2, Schedule 3, page 1 and Staff Interrogatory Response 24 b)

⁷ As shown in Exhibit 3, Tab 2, Schedule 1, page 6

“wholesale” values but in the Application they are treated as retail values for purposes of setting rates.

- The 2004 weather normalized values used to develop the NAC for each class are not the same as the weather normalized class sales presented later in the Application (see Exhibit 3, Tab 2, Schedule 6. Indeed, the numbers reported as being 2004 values in the first reference match the 2006 values in the later reference.

VECC encourages Hydro 2000 to clarify these issue in its Reply Submissions. VECC has no concerns or submissions regarding Hydro 2000’s proposed revenue offset of \$35,980.

Operating Costs

Total O&A costs for 2008 are projected to be \$244,817, up from a 2006 actual value of \$218,509⁸. Of the \$26,308 increase, over \$15,073 of this is due to the additional costs associated with the new Harris billing system⁹. VECC has reviewed OEB Staff’s Submissions¹⁰ on this issue and shares their concern as to whether this full amount can be viewed as truly incremental.

VECC also notes Hydro 2000’s revised proposal regarding the recovery of the costs associated with the preparation of its 2008 Rate Application. While Hydro 2000 has not formally requested a deferral account for such expenses, VECC submits that deferral of the estimated \$60,000 associated with the preparation of the current Application is appropriate. The purpose of the Cost of Service application is to provide a foundation for the Board’s 3rd GIRM in subsequent years. As a result, the expenditure should be viewed as an “investment” and amortized over these future years when the cost of preparing annual rate applications should be significantly lower.

VECC also agrees with the treatment of the recovery as a rate rider (as opposed to simple amortization as part of the revenue requirement). As the form the 3rd GIRM is still unknown, a rate rider offers more flexibility and ensures the appropriate amount is ultimately recovered.

VECC notes Board Staff’s query regarding the fact only \$40,000 has been “posted” to the deferral account. VECC assumes that the \$40,000 represents the amount spent to date (and deferred) but would welcome Hydro 2000’s explanation on the issue. Furthermore, VECC notes that Hydro 2000 did not respond to its query¹¹ for details regarding the services provided Deloitte and Elenchus. While the dollars have been removed from 2008 revenue requirement,

⁸ Updated Application, Exhibit 4, Tab 1, Schedule 2, page 1

⁹ Response to OEB Staff #1b)

¹⁰ OEB Staff Submissions, December 10, 2007, pages 2-3.

¹¹ VECC #14 a) and b)

VECC submits that such information should be provided to support recovery of the amounts deferred prior to approval of any rate riders.

VECC has no comments regarding Hydro 2000's proposed depreciation expense.

Losses

VECC has reviewed Board Staff's submissions on this topic and supports the need to clarify the differences between the calculated and proposed loss factors. VECC suggests that approval of loss factors slightly less than those calculated based on past experience may be appropriate, in anticipation of the analysis and feeder rebalancing Hydro 2000 will be undertaking this coming January¹².

Cost of Capital/Capital Structure

VECC notes that the Capital Structure proposed in Hydro 2000's Application¹³ reflects the direction of the Board in its Report on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors. With respect to the cost of debt, Hydro 2000 has quoted a rate of 5.8% in its Application¹⁴ and also in response to Board Staff¹⁵. However, VECC notes that in its 2006 Financial Statements the cost of the note payable to the Township of Alfred-Plantagenet is 5.5%. Also, 5.5% was the value used in the 2006 EDR. VECC submits that Hydro 2000 weighted average cost of capital should be based on a long term cost of debt of 5.5% and revised to 6.956%¹⁶ overall (compared to the proposed value of 7.104%).

Also, VECC has noted a number of discrepancies in the way interest and net income have been included by Hydro 2000 in the overall revenue requirement:

- Hydro 2000 reports a 2008 regulatory interest expense of \$20,333. However, this appears to be Hydro 2000 actual projected interest expense for 2008 as opposed to its deemed interest expense for regulatory purposes. Based on Hydro 2000's projected interest costs and deemed capital structure, the value should be \$22,420¹⁷. Based on VECC's submission for a long term debt rate of 5.5% the projected interest costs fall to \$21,317¹⁸.
- Hydro 2000 reports a net income of \$31,759. However, based on their proposed equity ratio of 46.7%, the net income after tax should be

¹² Board Staff #48

¹³ Updated Application, Exhibit 6, Tab 1, Schedule 2 page 1

¹⁴ Updated Application, Exhibit 6, Tab 1, Schedule 3, page 1

¹⁵ Board Staff #18 a)

¹⁶ VECC #19 a)

¹⁷ Rate Base (\$735,075) * Debt Rate (3.05%) – See Exhibit 2, Tab 1, Schedule 4 and Board Staff #18 a)

¹⁸ Assumes a debt rate applicable to rate base of 2.9%, per VECC #19 a)

\$29,771¹⁹. This change in net income will also impact on (and reduce) the calculated PILs requirement.

Overall, VECC submits that Hydro 2000's revenue requirement should be adjusted to reflect interests cost and net income consistent with a 6.956% weighted average cost of capital. The tax calculations should then be adjusted accordingly.

Deferral and Variance Accounts

VECC has no submissions with respect to Hydro One 2000's proposals regarding the disposition of existing deferral and variance account balances. Board Staff's submissions are fairly comprehensive and have canvassed the issues that the Board must consider.

With respect to Hydro 2000's request for a new deferral account to capture capital spending in future years (i.e., 2009 and 2010), VECC submits that the request is premature. Hydro 2000 was unable to respond to Board Staff's questions²⁰ regarding the actual operation of the account. However, this is not surprising, given that the posting to the account will depend on the structure of the Board's 3rd GIRM – which is still being developed. In VECC's view, the Board should decline to make a determination on this matter until after the 3rd GIRM has been established. At that time, the Board will be in a better position to determine a) whether such accounts are required and, if so, b) how they should be structured.

Cost Allocation

LV Charges

VECC agrees with Board Staff's submissions regarding the allocation of LV Charges to customer classes. Hydro 2000 has treated LV Charges as a part of Distribution costs as opposed to treating them as a pass through – per the 2006 EDR Model. The allocation of LV charges should be in proportion to the Retail Transmission Rate – Connection charges each class will experience based on 2008 rates and loads.

Smart Meters

The same problem exists for the Smart Meter adder of 26 cents/month. Hydro 2000 has treated the resulting revenues as a "distribution cost" for purposes of determining and adjusting its 2008 Revenue to Cost Ratios. In principle and, to be consistent with past Board practice, the Smart Meter rate adder separated out and then added back in after the base distribution rates have been determined in accordance with any planned revenue to cost ratio adjustments.

¹⁹ Rate Base * 4.05%, per Board Staff #18 a)

²⁰ Board Staff #29

Base Distribution Costs

In order to determine the revenues for each customer class consistent with a Revenue to Cost Ratio of 100%, Hydro 2000 has used the percentage allocation of costs to customer classes derived from the 2006 Cost Allocation filing and applied it to the 2008 revenue requirement²¹. In VECC's view this is not the correct approach. Such an approach only works if the billing quantities forecast for each customer class for 2008 are all directly proportional to the billing quantities used to generate the revenues in the 2006 Cost Allocation filing. A brief review of the 2006 and 2008 values reveals that this is not the case. In VECC's view, the correct approach is to calculate the revenues for each class based on 2008 volumes and the 2006 rates (exclusive of the smart meter adder and LV recovery built into the rates) consistent with the Informational Filing's revenues. Using the results to pro-rate the 2008 Base Distribution Revenue Requirement to customer classes, can then be viewed as yielding revenues for each class consistent with the Revenue to Cost ratios calculated in the Informational Filings. VECC submits that this is the proper starting point for any planned adjustment to more closely align Revenue to Cost Ratios with the Board's Guidelines and/or move closer to 100%.

Given the results of Hydro 2000's Cost Allocation Informational²² filing and the Board's Guidelines, VECC submits that Hydro 2000's first priority should be to move GS<50, Street Lighting and USL rates up to the lower end of range set by the Board for each class. The resulting increase in revenues would all be reallocated to the Residential class, the only class with a ratio over 100%. VECC considers any movement in the GS>50 class' Revenue to Cost Ratio to not be a priority matter at this time given that the ratio is at 94.5%, well within the range of reasonableness.

Rate Design

Hydro One 2000 proposes to increase the monthly service charge for the Residential class from \$8.20 to \$10.71²³. This represents an increase of over 30% - more than twice the increase in the proposed volumetric charge for residential customers²⁴. Hydro 2000 explains that the increase is designed to improve stability²⁵. VECC submits that there is no justification for this shift in the rate design of the Residential class at this time:

- The proposed \$10.71 is the upper end of the range for monthly service charges as calculated by Hydro 2000's Cost Allocation Informational Filing²⁶.

²¹ Board Staff #39 b)

²² Exhibit 8, Tab 1, Schedule 2

²³ Both values include the \$0.26 Smart Meter rate adder

²⁴ Updated Application, Exhibit 7, Tab 1, Schedule 1, page 2

²⁵ VECC #20 b)

²⁶ Updated Application, Exhibit 8, Tab 1, Schedule 2, page 3

- For the revised Application, which included a substantially lower revenue requirement for residential customers than the September 2007 filing, the proposed customer charge was held constant. In VECC's view this brings into question Hydro 2000's objective of maintaining a certain percentage of fixed vs. variable revenues. Rather it appears Hydro 2000's objective is to maximize revenue from fixed charges.
- The existing monthly charge of \$8.20 is comfortably within the range generated by the Cost Allocation Informational Filing.
- Rate stability and customer fairness, objectives supported by Hydro 2000²⁷, are not promoted by such significant shifts over a one year period.
- Finally, as noted by Board Staff, the Board is currently conducting a study of rate design principles with the expectation that fundamental changes will not be implemented until it completed.

Overall, VECC submits that the proportion of residential revenues collected from the 2008 fixed versus volumetric charges should remain unchanged from that generated by existing rates.

Recovery of Reasonably Incurred Costs

VECC submits that its participation in this proceeding has been focused and responsible. Accordingly, VECC requests an award of costs in the amount of 100% of its reasonably-incurred fees and disbursements.

Respectfully Submitted on the 16th Day of December 2007

Michael Buonaguro
Counsel for VECC

²⁷ See VECC #20