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January 21, 2011

VIA MAIL and E-MAIL

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

Dear Ms. Walli:

Re: Vulnerable Energy Consumers Coalition (VECC)
Preliminary Issue Submissions: EB-2010-0139
Norfolk Power Distribution Inc. – 2011 Electricity Distribution Rate Application

Please find enclosed the submissions of the Vulnerable Energy Consumers Coalition (VECC) on Norfolk Power's application for early rebasing in the above noted proceeding.

Thank you.

Yours truly,

Michael Buonaguro
Counsel for VECC
Encl.
cc: Ms Jody McEachran
Norfolk Power Distribution Inc.

EB-2010-0139

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 Norfolk Power Distribution Inc. pursuant to section 78 of the *Ontario Energy Board Act* for an Order or Orders approving just and reasonable rates for electricity distribution to be effective May 1, 2011.

PRELIMINARY ISSUE SUBMISSIONS

On Behalf of The

VULNERABLE ENERGY CONSUMERS COALITION (VECC)

January 21, 2011

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Vulnerable Energy Consumers Coalition (VECC)

Preliminary Issue Submissions

1 The Application

1.1 Norfolk Power Distribution Inc. ("Norfolk") filed an application ("the Application") with the Ontario Energy Board ("the Board"), under section 78 of the Ontario Energy Board Act, 1998 on October 28, 2010 for electricity distribution rates effective May 1, 2011. The Application was filed in accordance with the OEB's guidelines for a cost of service application.

1.2 On December 16, 2010 the Board issued Decision & Procedural Order No. 1 outlining that under the 3rd Generation Incentive Regulation Norfolk would normally have applied for rates on a cost of service basis for 2012. The Board also noted that in a letter sent to distributors on April 20, 2010 the Board had advised that "a distributor … that seeks to have its rates rebased in advance of its next regularly scheduled cost of service application must justify, in its cost of service application, why an early rebasing is required notwithstanding that the "off-ramp" conditions had not been met". In the same letter the Board also indicated that it "may consider it appropriate to determine, as a preliminary issue, whether the application for rebasing is justified or whether the application as framed should be dismissed". Therefore, in Norfolk's case, the Board indicated that it was going to consider Norfolk's application for early rebasing in 2011 distribution rates (the "Preliminary Issue") in advance of further procedural steps.

1.3 The following section sets out VECC's submissions regarding the Preliminary Issue.

2 Preliminary Issue – Early Rebasing

Background

2.1 In the Report of the Board on 3rd Generation Incentive Regulation the Board determined that the plan term would be three years (i.e., rebasing year plus three). The Board also indicated that "the rates of the distributor are not expected to be subject to rebasing before the end of the plan term other than through an eligible off-ramp"[1]. In this regard, the Report established a trigger mechanism with an annual ROE dead band of +/- 300 basis points with the requirement that distributors report in the event that the distributor falls short of or exceeds its ROE by 300 basis points. This report would then determine if further action by the Board is warranted, including early termination of the IRM plan[2].

2.2 As noted above, on April 20, 2010, the Board sent a Letter to all distributors stating:

> "A distributor, including the four distributors referred to above, that seeks to have its rates rebased in advance of its next regularly scheduled cost of service proceeding must justify, in its cost of service application, why an early rebasing is required notwithstanding that the "off ramp" conditions have not been met. **Specifically, the distributor must clearly demonstrate why and how it cannot adequately manage its resources and financial needs during the remainder of its IRM plan period** (emphasis added)**.** Distributors are advised that the panel of the Board hearing the application may consider it appropriate to determine, as a preliminary issue, whether the application for rebasing is justified or whether the application as framed should be dismissed".

2.3 On May 31, 2010, Norfolk wrote the Board indicating that "based on changes to its rate base and distribution revenue since it last rebased in 2008, it will meet the criteria for an "off-ramp" provision, earning less than its approved ROE, by more than 300 bps for the year 2011". In the same letter, Norfolk referenced the fact that it had also informed the Board on February 19, 2010 of its intention to file a cost of service application in August 2010 for rates effective May 1, 2011.

Norfolk's Early Rebasing Application

2.4 In its October 28, 2010 Application[3], Norfolk outlined its rationale of filing for early rebasing. This rationale was expanded on in response to Board Staff IR #2 where four specific reasons were presented:

- Rate Stabilization

[1] Page 7
[2] Page 38
[3] Exhibit 1/Tab 2/Schedule 1, pages 2-4

- Prior Board Decision
- Rate Application Efficiency
- Financial Need

VECC's submissions will address each of these areas.

- o *Rate Stabilization*

2.5 Under this heading Norfolk presents two reasons for early rebasing. The first is that with the completion of its new transformer station there is a significant reduction in the Retail Transmission Service Rates that need to be charged to customers which are not captured in the simplistic IRM-based adjustments to RTSRs[4]. Norfolk also argues that since its customers are now benefitting from the new transformer station through lower transmission charges, they should pay for the costs related to the new station.

2.6 With respect to the benefit of lower RTSR charges, these benefits will be tracked in appropriate RSVA variance accounts and refunded to customers. With respect to additional costs arising for the new transformer station, VECC notes Norfolk's confirmation that it would qualify for an Incremental Capital Module (i.e., exceed the materiality threshold) in 2011 and, indeed would have also qualified for one in 20105. As a result, in VECC's view, avenues existed under the IRM framework to address these matters and they are not compelling reasons why Norfolk could not stay on the IRM for another year.

2.7 The second reason cited by the company is that the disposition of its Group 1 deferral/variance accounts as approved in EB-2009-0238 results in refunds to customers in both 2010 and 2011. If the rebasing is delayed until 2012, the removal of the rate rider plus any increase in rates from the cost of service application will lead to rate volatility.

2.8 VECC submits that there is no evidence to suggest that if a cost of service review

[4] Board Staff #2, page 10
[5] Energy Probe #3 a) and b)

is delayed until 2013 that rate increases will be in excess of what the Board considers as acceptable without rate mitigation. Indeed, Norfolk has failed to acknowledge that with a 2013 cost of service application, there are likely to be reductions in the RTSRs and refunds associated with the related RSVA accounts that will help to mitigate any anticipated rate impacts due to such an application. Again, VECC submits that these reasons do not justify a departure, in 2011, from the IRM framework.

- *Prior Board Decision*

2.9 Norfolk claims that the Board, in its EB-2008-0238 Decision, acknowledged that Norfolk would be filing a 2011 cost-of-service based application and that this was part of the rationale for the Board accepting its proposal for refunding its Group 1 deferral/variance account balances[6]. Norfolk appears to also be suggesting, that in doing so, the Board agreed that a 2011 cost-of-service based application was appropriate.

2.10 The Board's EB-2008-0238 clearly indicated that Norfolk's original proposal for a four year refund period was unacceptable and that a one year period was generally preferred. The Board, in agreeing to Norfolk's proposed two-year refund period, indicated that the Company's rationale was reasonable and therefore could be viewed as having (implicitly) acknowledged Norfolk's plan to file a cost of service based application for 2011 rates.

2.11 However, VECC notes that there is a significant difference between acknowledging a distributor's "plan" to file a cost of service based application and accepting the application that is eventually filed as being appropriate. The 3rd Generation Incentive Regulation Report of Board clearly laid out the off-ramp requirements during the IRM term and that distributors would not be eligible for rebasing except other than through an eligible off-ramp.

2.12 VECC submits that it would have been reasonable for the Board to assume that

[6] Exhibit 1/Tab 2/Schedule 1, page 4 and Board Staff #2, pages 11-12

Norfolk, when indicating in its intention to file a cost of service based application during EB-2008-0238, would meet the prerequisite requirements for such an application. These requirements are discussed further below under the Section "Financial Need".

2.13 As a result, VECC submits that the Board's (implicit) acknowledgement in its EB-2008- 0238 that Norfolk planned to file a cost of service based application in 2011 is not grounds for making a determination that such an application is required. Indeed, in its April 20, 2010 letter the Board acknowledged that there were four distributors that had indicated their intention to file for early rebasing in 2011 and clearly stated that all four would be required to justify why such early basing was required, not withstanding that the off-ramp conditions had not been met. In VECC's view this letter negates any argument that acknowledgement of a pending cost of service application is equivalent to accepting the application as justified.

- *Rate Application Efficiency*

2.14 Norfolk submits that it is more efficient to proceed with a cost of service application at this time (followed by an IRM in 2012) than to file an IRM-based application for 2011 (followed by a cost of service application in 2012)[7]. The main argument appears to be that an IRM application in 2011 would have to be accompanied by applications for LRAM, RTSR, Smart Meters and an Incremental Capital module – all of which would add complexity to Application.

2.15 In VECC's view Norfolk is both overstating the complexity associated with an IRM application and also overstating the benefits of an early rebasing application from an efficiency perspective. With respect to an IRM application, Norfolk has agreed that LRAM and Smart Meter applications are not a mandatory part of the process[8]. Furthermore, an Incremental Capital Module is not necessarily controversial or requires an oral hearing as Norfolk suggests. Indeed, VECC is a registered intervenor for the proceedings of two distributors who have requested incremental

[7] Board Staff #2, page 13
[8] Energy Probe #4

capital modules for 2011 based on new transformer stations[9]. Neither application has given rise to an oral proceeding. Furthermore, while there have been questions regarding the calculations used in Incremental Capital Module, in both cases intervenors[10] have agreed (in principle) that the ICM application is appropriate.

2.16 VECC also notes that, since Norfolk has not completed its Smart Meter implementation as of December 31, 2009,[11] all smart meter costs will not be incorporated into rate base as pat of a rebasing application for 2011 rates. As a result, such an application will not eliminate the need for applications during the subsequent IRM period to potentially deal with Smart Meter adders. Similarly, there will be an ongoing issues regarding lost revenue due to CDM that Norfolk may choose to deal with as part of its future IRM applications.

2.17 VECC submits that Norfolk has not made a compelling case for increased regulatory efficiency. Also, VECC views it as ironic for Norfolk to be arguing for an early termination of its IRM term on the grounds of regulatory efficiency when this is one of the key reasons why IRM was introduced by the Board in the first place.

- *Financial Need*

2.18 Norfolk indicates that when it submitted its letter of May 31, 2010 confirming its intention to file a cost of service application for 2011 rates it expected to earn less than the approved ROE, by more than 300 bps, for 2011. Revisions to expected expenditures in 2011 have reduced this amount to 296 bps[12] relative to its 2008 approved ROE. However, Norfolk asserts, it's expected 2011 ROE (as current rates) is 424 basis points below the 9.85% deemed return on equity for 2010 rebasing applications[13]. Norfolk also indicates that it expects significant capital

[9] Oakville Hydro (EB-2010-0119) and Guelph Hydro (EB-2010-0130)
[10] VECC and the Schools Energy Coalition are intervenors in both proceedings
[11] VECC #3 d)
[12] Board Staff #2, page 14
[13] Exhibit 1/Tab 2/Schedule 1, page 2

expenditure to replace aging assets[14].

2.19 First, with respect to Norfolk's comparison of its forecast 2011 ROE versus the approved 2010 ROE, VECC notes the Board's findings with respect Hydro Ottawa's 2011 cost of service application that "a cost of service application provides an opportunity to implement the Board's policies in these areas, but the policies themselves are not a reason to advance a cost of service application early"[15]. As a result, VECC submits that it is clear that the appropriate ROE to use in establishing whether or not the prescribed 300 bps off-ramp has been triggered is the ROE approved for Norfolk in its last cost of service application – 8.57%.

2.20 VECC also submits that off-ramp was meant to be triggered based on actual financial results as opposed to forecast results. The Board's 3rd Generation Incentive Regulation report clearly states[16] that "when a distributor performs outside this earnings dead band, a regulatory review may be initiated". This point is also obvious from the Board's requirement that "in support of this approach, a distributor will be required to make a report to the Board no later than 60 days after the company's receipt of its annual audited financial statements". Also, from a purely pragmatic perspective, it would be unreasonable for the Board to accept as evidence of the need for a cost of service application evidence/information (such as a forecast ROE for the test year) that could only be verified through a formal review of the entire application.

2.21 VECC submits that, with respect to the Board's prescribed off-ramp of 300 bps what is important is Norfolk's actual ROE to date during the IRM period. Norfolk's adjusted return on deemed equity for 2009 was 8.22% (well within the 300 bps dead band)[17].

2.22 Furthermore, although not actual results and clearly not audited, Norfolk's

[14] Board Staff #2, page 14
[15] EB-2010-0133 Decision, page 11
[16] Page 38
[17] Board Staff #1 c)

anticipated return for 2010 is 6.73% - again within the 300 bps dead band[18].

2.23 Finally, the 296 bps variance quoted by Norfolk for 2011 is misleading as its calculation includes the cost of smart meters in rate base. If smart meter costs are excluded and continue to be tracked in deferral/variance accounts as is currently the practice, the forecast return on deemed ROE for 2011 is 7.06%[19] - again well within the dead band.

2.24 Also, Norfolk appears to be fully able to manage its financial needs. The Company has indicated that it's been able to obtain the long term debt financing it required in 2009 and 2010 from third parties and has been able to do so without paying any premium over market rates[20].

2.25 VECC submits that Norfolk has not met the Board's prescribed off-ramp requirements and has not demonstrated that it cannot adequately manage its resources and financial needs during the remainder of its IRM plan period.

- *Summary*

2.26 Overall, it is VECC's submission that Norfolk has not justified the need for an early rebasing. When critically assessed, none of the reasons put forward justify, either individually or when taken in whole, why Norfolk should not stay on the IRM framework for 2011 as per the Board's original plan.

3 <u>Recovery of Reasonably Incurred Costs</u>

3.1 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.

All of which is respectfully submitted this 21st day of January 2011.

[18] Board Staff 1 e)
[19] Board Staff #1 b), page 6
[20] Energy Probe #6 a) and b)