Ontario Energy Board | **Commission de l'énergie de l'Ontario**

Ontario

EB-2009-0266

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 Hearst Power Distribution Company Limited for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2010.

BEFORE: Marika Hare
Presiding Member

Ken Quesnelle
Member

DECISION

February 15, 2011

BACKGROUND

Hearst Power Distribution Company Limited ("Hearst Power" or the "Applicant") filed an application with the Ontario Energy Board (the "Board") on April 28, 2010, under section 78 of the *Ontario Energy Board Act*, *1998*, S.O. 1998, c. 15, (Schedule B) (the "Act"), seeking approval for changes to the rates that Hearst Power charges for electricity distribution, to be effective May 1, 2010. The Board assigned File Number EB-2009-0266 to this application.

Hearst Power is a licensed electricity distributor serving approximately 2,750 customers in the Town of Hearst. It is one of over 80 electricity distributors in Ontario regulated by the Board. In 2006, the Board announced the establishment of a multi-year electricity distribution rate-setting plan for the years 2007-2010. In an effort to assist distributors in preparing their applications, the Board issued the *Filing Requirements for Transmission and Distribution Applications* on November 14, 2006, amended May 27, 2009.

On January 29, 2009, the Board informed Hearst Power that it would be one of the electricity distributors to have its rates rebased for the 2010 rate year. On April 28, 2010 (amended on May 21, 2010), Hearst Power filed a cost of service application based on 2010 as the forward test year.

The Board issued a Notice of Application and Hearing dated June 11, 2010. The Board approved the Vulnerable Energy Consumers Coalition ("VECC") as an intervenor. No letters of comment were received by the Board.

In Procedural Order No.1, issued on July 9, 2010, the Board made provision for preliminary interrogatories to clarify certain pre-filed evidence and indicated that after review of the responses to the interrogatories, it would determine the next steps. VECC and Board staff filed interrogatories. Hearst Power filed its responses to the interrogatories on September 15, 2010, and October 1, 2010.

In Procedural Order No.2, issued on October 6, 2010, the Board determined that it would proceed by way of a written hearing and made provision for a round of written supplemental interrogatories due by October 15, 2010. Submissions from Board staff and VECC were due by November 19, 2010, and a reply submission from Hearst Power was due by December 3, 2010. VECC and Board staff filed supplemental interrogatories by October 14, 2010. On October 28, 2010, Hearst Power requested an extension to file their responses to the supplemental interrogatories and on November 15, 2010, requested a further extension. Hearst Power filed responses to the supplemental interrogatories on November 22, 2010, and additional spreadsheet files on December 9, 2010.

In Procedural Order No.3, issued November 24, 2010, the Board noted that due to the late filing of interrogatory responses, it was necessary to modify the dates set out in Procedural Order No.2. Submissions from Board staff and VECC were reset as due by December 13, 2010, and a reply submission from Hearst Power by January 4, 2011.

On December 13, 2010, Board staff and VECC filed their submissions and on January 6, 2011 Hearst Power filed its reply submission.

Hearst Power originally requested a Service Revenue Requirement of $1,184,796[1] and a Base Revenue Requirement of $1,065,866. The proposed rates were set to recover a grossed-up revenue deficiency of $205,773[2]. In its reply submission, Hearst Power proposed a Service Revenue Requirement of $1,265,046 and Base Revenue Requirement of $1,196,139. The changes reflect increases in Hearst Power's rate base, return on rate base, PILs and OM&A costs, and decreases in amortization and the revenue offset. These adjustments reflected corrections and clarifications arising from responses to interrogatories.

The requested rate increase was estimated to be 11.08%[3] on the delivery component of the bill for a residential customer consuming 800 kWh in the winter and summer months. The total bill impacts were moderated by the inclusion of deferral and variance account balances that are in a credit position; as a result, the application showed a total bill increase of 2.73% ($2.33 per month) for these Residential customers. Hearst Power did not provide updated estimates of bill impacts in its reply submission.

The full record is available at the Board's offices. The Board has chosen to summarize the record to the extent necessary to provide context to its findings.

[1] Exhibit 8, Tab 1, Schedule 1, Page 1
[2] Exhibit 6, Tab 1, Schedule 1, Page 1
[3] Exhibit 8, Tab 1, Schedule 5, Page 2, Table 8.1.5.3

THE ISSUES

The following issues were raised in the submissions of Board staff and the intervenor, and are addressed in this Decision:

- Effective date for new rates
- Rate Base and Capital Expenditures
- Customer / Load Forecast and Revenues
- Operating Costs
- Cost of Capital and Rate of Return
- Cost Allocation and Rate Design
- Deferral and Variance Accounts

EFFECTIVE DATE FOR NEW RATES

In its application, Hearst Power requested that the Board issue an interim Order approving its proposed distribution rates and other charges effective May 1, 2010. In its Decision and Order on Interim Rates, dated June 24, 2010, the Board did not approve Hearst Power's proposed rates on an interim basis. The Decision and Order stated that were such approval granted, it might be perceived as pre-empting the outcome of the Board's review of Hearst Power's application, and would likely result in implementing further rate changes because the elements of the application had not yet been tested for prudence.

The Board determined that Hearst Power's current distribution rates should be declared interim as of May 1, 2010. The Board also stated that it would determine at a later date, if the new rates should be effective as of May 1, 2010, or as of a later date. By granting rates interim as of May 1, 2010, the Board noted, it had retained the authority to make the final rates effective as of that date, but that it is not required to do so.

In the interrogatory process, Board staff referenced[4] the Board's March 5, 2009, letter which advised all electricity distributors that "Applicants are encouraged to file applications for 2010 as soon as possible, and no later than August 29, 2009 for rates to become effective May 1, 2010." Hearst Power was asked to explain the reasons for the late filing of its Application. Hearst Power explained that it had advised the Board that it would be unable to meet the August 15, 2009 filing deadline because of the necessity to address Board mandated programs and local issues. Moreover, as a small and first-

[4] Board staff supplemental interrogatory #3

time cost of service applicant, it had not expected the exercise to be such a time consuming exercise for its internal resources.

In its submission, Board staff noted that Hearst Power was advised in the Board's April 20, 2010 letter that if it did not file its cost of service application by April 30, 2010, then its application should be filed as a 2nd generation IRM application. Board staff noted that by not filing its Application until May 21, 2010, Hearst Power's was almost nine months late. Had Hearst Power complied with the directions in the Board's April 20, 2010 letter, it should have filed a 2nd generation IRM application.

Board staff submitted that when a utility fails to file a complete and accurate application by the required deadline, it forfeits its right to expect its new rates to be effective by May 1 of the following year. Board staff further submitted that consistent with the Renfrew Decision (EB-2009-0146), the effective date should be the beginning of the month after the issuance of the Decision.

VECC submitted that the effective date should be no earlier than October 1, 2010, which it considered to be generous. It listed effective dates later than October that might be warranted by the delays at the outset and during the proceeding, and suggested that the Board needs to send a clear signal to all applicants that not filing on time has consequences.

VECC also pointed out that the implementation date might be later than the effective date, and that there could be relatively few months remaining in the rate year to recover revenue foregone between the effective and implementation dates. It suggested that consideration should be given to extending the recovery period over a longer period than the end of the rate year.

In its reply submission, Hearst Power disagreed that there would be any value in sending a signal to other distributors concerning late applications and missed deadlines, and reiterated the circumstances that have made it difficult for Hearst to comply with the same schedule as larger distributors. It submitted that an effective date suggested by Board staff, being February 1, 2011 at the earliest, would impose a considerable loss in revenue. It recommended September 1, 2010 as a compromise that would result in a manageable loss to the utility.

Board Findings

The Board in its Decision and Order on Interim Rates issued on June 24, 2010, stated that by making rates interim as of May 1, 2010, the Board preserves the ability to make the final rates effective as of that date, but not the requirement to do so.

Board staff submitted that the effective date of new rates should be the beginning of the month following the Board's Decision. VECC submitted a rationale for an effective date of October 1, 2010, or later. The Applicant submitted that September 1, 2010 would be reasonable.

The Board considers the timelines it establishes for filing future test year cost of service applications to be in the public interest. The timelines allow a reasonable time for the hearing of the matter before it and provide appropriate public notice as to what may occur in the future as a result of the hearing. The Board notes that Hearst Power was required to file its 2010 cost-of-service rates application by August 28, 2009 in order to have rates effective May 1, 2010. The Board set this date in order that Hearst Power would be fully aware of the time required to process an application and could therefore plan accordingly. Further, in its letter dated April 20, 2010, the Board advised Hearst Power that if it did not file its cost-of-service application by April 30, 2010, then its application should be filed on the basis of a 2nd generation IRM. Hearst Power was eight months late in filing its application. The preparation and filing of a cost of service rebasing application should be considered a core activity for a distributor. The setting of rates based on a public hearing of the underpinning basis for the proposed revenue requirement is the manner in which the merits of the distributor's planned activities are tested. The time frame of this proceeding has eclipsed the future test year that it is based on.

The Board has therefore determined that Hearst Power's new rates will become effective on February 1, 2011

RATE BASE AND CAPITAL EXPENDITURES

Hearst Power requested approval of $2,355,582 as the 2010 Rate Base[5]. This amount was made up of net fixed assets (i.e. Average Net Book Value) of $1,295,485 and a Working Capital Allowance of $1,060,098.

[5] Exhibit 2, Tab 1, Schedules 1-3

In interrogatory responses[6], Hearst Power modified its 2010 Rate Base value to $2,944,609. Most of the increase was attributable to an increase in power supply expenses, and minor revisions to the Rate Base were made as individual components were updated through the discovery process.

In its reply submission, Hearst Power modified its proposed rate base to $2,385,912. The following table shows the resulting trend in annual amounts that would comprise the rate base.

Table 1 – Rate Base Trend ($ million)

Year	2006 Actual	2007 Actual	2008 Actual	2009 Projection	2010 Forecast
Total Rate Base	$2.295	$2.210	$1.961	2.164	$2.386

The following issues are addressed in this section:

- Smart Meters
- Capital Policies and Plan
- Accumulated Amortization
- Working Capital Allowance
- Service Quality and Reliability Performance

Smart Meters

Board staff noted that the Applicant's treatment of Smart Meter-related capital expenditures in its pre-filed evidence[7] was unclear. It was noted that Smart Meters and their supporting communication systems appear to have been included in the Applicant's rate base in a manner that is not consistent with the Board's G-2008-0002 Guideline: Smart Meter Funding and Cost Recovery, October 22, 2008 (the "Guideline"). For example, the cost information was not audited in the manner required by section 1.5 of the Guideline. Hearst Power reiterated[8] that since 100% of its smart meters would be installed by end of 2010, it considered it was eligible to recover its costs through its Rate Base and regular OM&A expenses.

[6] Board staff interrogatory #2 and VECC interrogatory #6
[7] Exhibit 2, Tab1, Schedule 3, page 2
[8] Board staff interrogatory # 4 and Board staff supplemental interrogatory #36

Board staff suggested that it would be appropriate for Hearst Power to include in the rate base the audited costs of the smart meters installed in 2009. The residual balances associated with the 2009 smart meter installations captured in deferral accounts 1555 and 1556 should be disposed of by means of a disposition rate rider. With respect to smart meters installed in 2010, Board staff disagreed that these costs should be included in the rate base since the cost information is not audited and doing so would be counter to the Board's Guideline referenced above. Board staff took the position that, pursuant to section 1.6 of the Guideline, it would be appropriate for Hearst Power to seek recovery of smart meters installed in 2010 by means of a smart meter disposition rider once the financial information has been audited.

VECC took the same position as Board staff concerning 2010 expenditures. VECC submitted that capital spending to the end of 2009 should also be excluded from rate base at this time and continue to be included in deferral accounts due to ambiguities that it identified in the record, and a smart meter adder established accordingly.

In its reply submission, Hearst Power indicated that it no longer seeks approval to transfer into its rate base the capital cost of smart meters installed in 2010. As for the 2009 data, it submitted that there is no inconsistency, after clarifying gross versus net book values, correcting for a typographical error, and making a clearer distinction between smart meters and ordinary meters. There is therefore no reason, in the Applicant's submission, to not use the audited data as per the auditor's letter dated February 25, 2010[9] and to transfer the 2009 balance to Hearst Power's rate base.

Capital Policies and Plan

Hearst Power proposed[10] a capital expenditure of $248,696 in 2010. A summary of its 2006-2010 capital expenditures is shown in Table 2 below.

Table 2 – Capital Expenditures ($k)

Year	2006	2007	2008	2009	2010
Capital Expenditures	58	52	115	463	249

Hearst Power showed[11] that it had included its smart meter spending in its 2009 and 2010 capital expenditures; the smart meter components included were stated to be $437k (2009) and $115k (2010). The remaining 2010 expenditures focus on replacing

[9] VECC interrogatory # 32(d), Appendix X
[10] Exhibit 2, Tab 5, Schedule 1
[11]Exhibit 2, Tab 5, Schedule 1

poles, transformers and installing transformer pads for underground distribution. No expenditure is included in this application in support of the government's Green Energy initiative.

Board staff noted in its submission that the 2010 capital expenditure proposed in the application represents a 47% decrease from 2009 which, in turn, was a 310% increase from 2008. The fluctuations were seen to be primarily a result of the inclusion of smart meter costs in 2009 and 2010.

In order to focus on the issue of non-smart meter capital expenditures, Board staff presented Table 3 below, based on updated data provided by the Applicant[12]. The items specifically identified by Hearst as smart meter related were excluded.

Table 3 – Capital Expenditures Excluding Smart Meters ($k)

Year	2006	2007	2008	2009	2010
Capital Expenditures excluding smart meters	58	52	115	45	134

Hearst Power clarified[13] the matter with additional information on capital expenditures that are slightly higher than usual yet still fall below the materiality threshold:

- The $13,000 in Buildings and Fixtures related to the warehouse roof to be replaced,
- The $25,000 spending on Office Furniture and Equipment – folding machine,
- The $25,000 spending on Software – Smart Meter related software (MDMR), and
- The $12,500 spending on Transportation Equipment – Maintenance on trucks.

Board staff stated that it does not have an issue with the necessity of any of the 2010 proposed expenditures even though the 2010 total is a significant increase from the historical norm. However, Board staff noted that the $25k software is "smart meter-related" and the $12.5k amount is for truck "maintenance". Thus, Board staff invited Hearst to verify that:

- the "smart meter software" is for the processing of data (e.g. billing) after the data have been received by the utility (otherwise the software should be considered a smart meter expenditure and be accounted for in a similar manner to smart meters), and

[12] Appendix H provided in response to VECC interrogatory #8
[13] Board staff supplemental interrogatory #15

- o the "maintenance" performed on the trucks is a betterment that increases the resale value of the trucks and not regular maintenance which keeps the vehicles in running order (and would therefore be an OM&A cost).

VECC agreed that Hearst Power's proposed capital expenditures were reasonable to include in the rate base, noting that the capital program over several years had consisted largely of smart meters and that the apparently high expenditures in 2010 were catching up. VECC expressed concern about the amount included in the capital program for PST (as well as in OM&A), and suggested methods by which PST savings after July 1, 2010 could be removed from the rate base.

Hearst Power confirmed in its reply argument that the software is related to MDMR rather than smart meters per se, and that the expenditures on the trucks will increase the resale value. Concerning the PST, Hearst Power pointed out that it had paid PST while it was in effect in the first half of 2010, and submitted that the amount should be recorded in a deferral account to be recovered later.

Accumulated Amortization

Hearst Power acknowledged[14] that it had not consistently applied the half year rule throughout the historical years, but submitted that it had updated its depreciation as directed in the minimum filing guidelines. Hearst Power corrected and updated its evidence[15] with respect to depreciation charges for 2010 and prior years in its responses to initial and supplemental interrogatories.

In its submission Board staff said that it remained uncertain about whether the half year rule had been applied consistently by Hearst Power. VECC noted that the historical application of the half year rule affects only the most recent year, and that capital additions in 2009 had been very small (except for smart meters, as discussed above).

In its Reply Submission, the Applicant submitted that with the 2010 smart meters removed its Net Fixed Assets are $1,228,149. It noted that VECC was in agreement with the proposal, and it addressed Board staff's concern by confirming that it had applied the half year rule correctly.

[14] Board staff interrogatory #7
[15] VECC interrogatory #19; Appendix 2IR_D provided in response to Board staff interrogatory #13

Working Capital Allowance

In its application, Hearst Power's proposed Working Capital for the 2010 Test Year was $7,067,318[16] which translated to a Working Capital Allowance ("WCA") of $1,060,098.

In an interrogatory response[17], Hearst Power reduced the cost of power to $5,409,909 with a corresponding reduction in WCA. Hearst Power showed that the 15% WCA factor had been correctly applied.

Board staff submitted that it had no issue with the WCA value provided it had been calculated on the basis of the latest-filed load forecast in Appendix 2IR_C filed on November 22, 2010. Board staff stated that the resulting value of the WCA calculated on this basis was unclear. Board staff invited Hearst Power to confirm that the WCA value it was relying on was $1,165,797, which was provided in response to VECC supplemental interrogatory #38. If it should be a different value, Board staff suggested that calculations showing the determination of the WCA amount should be filed.

VECC noted an apparent discrepancy between the explanation of the commodity cost for power delivered to RPP customers, versus the values actually used in the calculation. Hearst Power responded that the cost of power it had used for RPP customers was the same as was used by other applicants who had filed draft rate orders in December 2010.

Service Quality and Reliability Performance

Hearst Power showed[18] that its Service Quality Indicators exceed SQI standards. Its service reliability statistics (SAIDI: System Average Interruption Duration Index and SAIFI: System Average Interruption Frequency Index) indicated that the frequent and long-duration outages in the service area were substantially the result of Hydro One outages, while Hearst Power's own performance in this regard was satisfactory. In an interrogatory response[19], Hearst Power provided statistics which excluded the Hydro One influence. Excerpts from the response are provided in Tables 4 and 5.

[16] Exhibit 2, Tab 1, Schedule 2, page 2 and Exhibit 2, Tab 4, Schedule 1
[17] Board staff supplemental interrogatory #9
[18] Exhibit 2, Tab 7, Schedules 1-2
[19] Board staff supplemental interrogatory #11

Table 4 – Reliability Statistics (*including* Hydro One effect)

YEAR	SAIDI -Annual	SAIFI - Annual
2006	10.73	5.79
2007	11.73	5.91
2008	1.20	0.95
2009	6.66	10.32

Table 5 – Reliability Statistics (*excluding* Hydro One effect)

YEAR	SAIDI -Annual	SAIFI - Annual
2006	1.60	0.98
2007	0.65	0.92
2008	1.20	0.95
2009	5.67	3.45

Board staff noted that there was a significant increase in both outage duration (SAIDI) and outage frequency (SAIFI) values for 2009. It submitted that no evidence was provided to explain the sudden large increase, and thus questions arose regarding the soundness of Hearst's distribution system and the ability of Hearst's field resources to rectify outages. In addition, Hearst Power modified[20] its 2005-2008 Total Loss Factor which averaged 1.0443, to include 1.0563 for 2009. Board staff submitted that the Applicant had not provided a full explanation of the apparent diminishing health of its distribution system in determining its capital expenditures and OM&A.

Hearst Power replied that its system is reliable and that the statistics are picking up supply outages upstream of its system. It plans to review its accounting reporting procedures to ensure that the distinction will be made correctly.

Board Findings

The Board notes that Board staff and VECC supported the net fixed asset portion of Hearst Power's rate base, with the withdrawal of 2010 smart meters and with the half-year rule correctly applied. The Board accepts Hearst Power's submission of the average balance of net fixed assets.

As noted above, in its final submission Hearst Power withdrew its proposal to transfer the smart meters installed in 2010 into its Rate Base. Hearst Power submitted that the balance at the end of 2009 should be included in its rate base, citing the letter from

[20] Board staff supplemental interrogatory #34

Hearst Power's auditor dated February 25, 2010. Board staff and VECC agreed with this submission. However, the Board will not approve the transfer of any of the balance in account 1555 to Hearst Power's rate base in this Decision. The Board considers that the requirements of the Guidelines G-2008-0002, section 1.5 have not been fully satisfied in the record before the Board. Several requirements outlined in the Guideline have not been filed or contain insufficient detail, precluding the Board from assessing whether these costs were prudently incurred. While not approving the transfer of the costs of smart meters installed in 2009 into rate base, the Board does make provision for partial recovery of smart meter costs later in this Decision.

In response to Board staff concerns about proposed capital spending on items of software and on transportation equipment, Hearst Power confirmed that the software expenditure would not be included with smart meters, and that the expenditure on equipment will increase the resale value of the assets. With this confirmation, the Board agrees that the expenditures in question shall be included in Hearst Power's rate base.

Hearst Power sought to record PST amounts actually paid in the first six months of 2010 in a deferral account for future recovery. VECC submitted an alternative approach but did not object to Hearst Power's proposal. The Board approves Hearst Power's proposal to remove the PST paid on the 2010 capital additions and record actual PST paid in the first six months of 2010 in a deferral account for future recovery.

Hearst Power submitted a Working Capital Allowance (WCA) for the 2010 test year of $1,163,143, which was based on 15% of the forecast cost of power and controllable expenses.[21] The Board notes that neither VECC nor Board staff objected to the WCA requested. The Board expects that the Applicant will include a detailed calculation of the updated WCA with its Draft Rate Order. The update will include Hearst Power's transmission costs and if necessary, its forecast of Low Voltage costs, as directed later in this Decision.

The Board notes that the reliability statistics suggest that 2009 was a poor year for both Hearst Power's own system and Hydro One's systems upstream from Hearst. The Board will be interested in its distribution reliability statistics in future years.

CUSTOMER / LOAD FORECAST AND REVENUES

The following issues are addressed in this section:

[21] Excel file 'Hearst_Rate Model_ SUPPIRS_20101209', submitted December 9, 2010

- Customer and Load Forecasts
- Throughput, Distribution and Other Revenues

Customer and Load Forecasts

Hearst Power initially filed a forecast of its customers/connections in the test year at 3,503. Board staff observed that the number of customers/connections had remained virtually constant at 3,705 over the 2006-2008 period, dropping to 3,680 in 2009 and increasing to 3,686 in the 2010 forecast[22]. The forecast was corrected to 3686, based on a stable number of customers, a small increase in the number of streetlight connections, and a gradual decrease in the number of sentinel light connections. Board staff expressed its view that the proposed customers/connections forecast is reasonable.

Hearst Power used a variation of the Normalized Average Consumption (NAC) approach to develop its 2010 load forecast in its application[23]. It was initially unclear whether the methodology included explicit weather normalization, or was based on data averaged over several years. The load was variously expressed[24] as a "2010 Test Year Forecast" of 86,167,555 kWh and a "2010 Test Year Weather Normalized (forecast)" of 116,205,364 kWh[25].

The Applicant confirmed that classes with weather sensitive loads were handled differently from those whose load is not affected by weather. It confirmed that the load forecast of weather-sensitive classes was a five year-average, and was not based on the weather-normalized loads provided by Hydro One in 2006.[26] Board staff noted that most utilities that develop a weather normalized load forecast achieve this by incorporating heating degree days and cooling degree days; Board staff submitted that a forecasting methodology like Hearst Power's, that does not use any weather normalization and does not consider trends in usage, is not sound.

On September 30, 2010, Hearst Power filed an "Addendum to Cost of Service Application EB-2009-0266" that contained "an alternate load forecast" of 77,587,715 kWh. The principal change in the filing was that the initial forecast of the Intermediate

[22] VECC interrogatory #10, and Board staff supplemental interrogatories, Appendix 2IR_F
[23] Exhibit 3, Tab 2, Schedules 1-4
[24] Exhibit 3, Tab 2, Schedule 3, page 4
[25] Board staff interrogatory #8
[26] Board staff supplemental interrogatory #17

class had included the assumption that load lost in 2007-2008 would be regained in the test year, but subsequent events proved that assumption to be inaccurate.

From Hearst Power's comparison of the 2010 kWh forecast and the 2010 kWh actual usage to date[27], Board staff concluded that, on a proportional basis, the forecast value is just slightly higher than the trending actual. This observation together with the explanation provided by Hearst that there appeared to be little chance that the recently shut-down production lines would re-open in the foreseeable future, led Board staff to conclude that the proposed load forecast result is reasonable. Board staff therefore submitted that the 77,587,715 kWh load forecast should be approved by the Board.

VECC noted that Hearst Power's load forecast is 2.6% below the actual usage in 2009. However, it acknowledged that weather normalization requires an intensive effort, and submitted that the forecast should be accepted as modified for 2010. It suggested that the Board should encourage Hearst Power to explore other approaches to load forecasting for use in its next cost-of-service application.

Throughput, Distribution and Other Revenues

Hearst Power forecast Other Revenues (i.e. Revenue Offsets) for 2010 to be $118,930[28]. This amount is used consistently in the application, notably in the Revenue Requirement Work Form and in the Cost Allocation model. However, the proposed amount was subsequently reduced to $68,907 by Hearst Power[29].

Board staff stated that most of the components of Other Revenues were reasonably stable over the historical and forecast periods, or that there were intuitive explanations for changes (e.g. low interest rates for investments). Board staff noted that additional information[30] supported the reasonableness of components of the revenue offset within the original amount. VECC submitted that the revised amount was in line with previous years.

VECC however also expressed a number of concerns with Hearst Power's accounting with its affiliates. In particular Hearst Power provides labour for street light maintenance, to be performed in future by Hearst Power Sales and Service, but

[27] Board staff supplemental interrogatory #19
[28] Exhibit 3, Tab 3, Schedule 1
[29] VECC interrogatory 11a and Appendix N
[30] Board staff supplemental interrogatory #21

appears to not include any payment for such services in its revenue offset.[31] In the absence of more specific information, VECC submitted that the Board should direct Hearst Power to provide clearer explanations of its costs and revenues associated with its affiliates, both with the Town of Hearst and with Hearst Power Sales and Service.

Hearst Power replied that the confusion appears to involve posting amounts to account 4235 instead of 4325. It plans to have a consultant review its internal accounting procedures.

Board Findings

The Board has based most distribution rate decisions on a load forecast of weather-sensitive loads that is weather-normalized, and based on a lengthy record of weather and load information. The Board is sympathetic to the argument that trending of average consumption data would produce a more meaningful load forecast than one based on averages.

The Board notes that Board staff and VECC agreed that Hearst Power's forecast of 3686 customers and 77, 587,715 kWh was reasonable. The Board accepts this forecast and the forecasts of billing quantities that are based on them.

The Board agrees with VECC's submission that Hearst Power should explore improved methods of load forecasting for its next cost-of-service application. Hearst Power should be mindful of the need to weigh the cost and associated rate impacts of achieving a more robust forecast against the benefits gained.

With respect to the proposed revenue offset, the Board notes that the larger amount of Revenue Offset submitted in the original Application was not supported by detailed evidence, whereas the revised lower amount is supported in the interrogatory response. VECC submitted that the revised amount was consistent with the amounts recorded in previous years. The Board approves the proposed revenue offset of $68,907.

[31] Response to VECC supplemental interrogatory # 47(b)

OPERATING COSTS

The following issues are addressed in this section:

- Operating, Maintenance and Administration Expenses (OM&A)
- Income and Capital Taxes

Operating, Maintenance and Administration Expenses

In its application[32], Hearst Power requested approval of $867,878 for total OM&A expenses for the 2010 test year. It clarified certain ambiguities and provided a consistent set of historical and forecast OM&A details[33], and revised its OM&A forecast to $935,399. A summary of the updated data[34] is shown in Table 6.

Table 6 – Summary of OM&A Expenses

	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Forecast
OM&A Expenses	$641,459	$665,483	$695,799	$802,639	$935,399

Hearst Power explained that the additional costs it will incur in 2010 include the meter reading program in support of smart meters, an additional employee in preparation for a planned retirement and the increased costs resulting from a negotiated labour settlement.

Hearst Power leases office space from the Town of Hearst and the utility in turn provides water meter reading and billing services, street light maintenance and related services to the Town. Hearst Power provided details of the monetary value of a number of its Purchased Services.

Hearst Power also filed evidence[35] that showed the portion of the utility's wages that was used to provide support activities for the Town of Hearst which was fully paid for by the Town. Board staff examined Hearst Power's affiliate relationships and concluded it had no issue. It also followed up[36] on details of the tendering process for a number of Hearst Power's larger expenditures and submitted that it had no issue.

[32] Exhibit 4, Tab 2, Schedule 1, page 1
[33] Board staff interrogatory #10 and VECC interrogatory #13
[34] Appendix BS-G and Board staff supplemental interrogatory #23
[35] VECC interrogatory # 17
[36] Board staff supplemental interrogatory #28

Board staff calculated that total compensation increased by 3.0% per annum over the 2006-2010 period. Hearst Power reported[37] it had used a zero inflation rate for its non-labour expenses in 2009 and 2010, and the inflation rate used for the 2010 OM&A forecast[38] was not a specific inflation factor but rather each account had been looked at individually.

Board staff noted that OM&A during the 2006-2008 period increased by 4.2 % per annum, from 2008 to 2009 OM&A increased by 15.4%, and from 2009 to 2010 OM&A is forecast to increase by 16.5 %. Measured over the 2006-2010 period, the average increase was noted to be 11.5 % per annum.

Hearst Power showed[39] its OM&A expenses up to September 30, 2010, totaled $535k, which as Board staff noted would equal a full-year expenditure of $713k on a proportional basis. Hearst Power emphasized that it had "held off on most of its 2010 spending until the proposed revenue requirements is approved". The extrapolated 2010 year-to-date expenditure of $713k would be an 11.2% reduction from the 2009 actual.

Hearst Power stated[40] that additional OM&A cost drivers from 2008 to the 2009 bridge year included the use of outside services in support of its rebasing application ($108k was the 2009 component) and employee pension and benefits resulting from resolution of an earlier strike ($83k). From 2009 to 2010, a main cost driver was associated with the reading of smart meters ($52k).

In an interrogatory response[41], Hearst Power provided detailed calculations of its regulatory costs, comprised of a revised rebasing cost estimate of $207,649 and IRM estimate of $62,436, which together totaled $270,085. The response stated that $67,521 (i.e. $270,085 / 4) had been added to the Outside Services account, bringing the total OM&A from its previous value of $867,878 to $935,399. Board staff noted however, that it appeared that in Hearst Power's response, $76,516 (not $67,521) had been added to the 2010 OM&A expenses to achieve the $935,399 total. This suggested to Board staff that the total regulatory amount was $306,064.

[37] VECC interrogatory #14
[38] Board staff supplemental interrogatory #23
[39] Board staff interrogatory #23 and Appendix 2IR_G
[40] Appendix 2-H
[41] VECC interrogatory #15

Hearst Power clarified that the apparent discrepancy in regulatory costs identified by Board staff is due to $8995 per year for regulatory consulting needs other than rate applications, and that the total is $76,516 when this amount is included.

Regarding OM&A expenses, Board staff suggested that the very large percentage increases that Hearst Power had experienced – and expected to experience – were attributable to expenditures which would be of the same dollar magnitude for any utility. They appear to be excessive in percentage terms for Hearst because of its small size. For example, Board staff noted that Hearst Power had reported[42] that, in anticipation of an expected retirement, it hired an apprentice line maintainer at a cost of $91k in 2010 – this is 9.9% of its 2010 OM&A cost. (Hearst Power stated[43] that its apprentices are trained outside of Hearst and that the $91k included travel and accommodation costs.) Similarly, Board staff noted that the cost to obtain external assistance for its current rebasing was not dissimilar to that for much larger utilities but, again, represented a much larger percentage increase for Hearst Power.

VECC questioned whether PST expenses in the proposed revenue requirement are for a full year and that savings in PST after mid-year 2010 may not have been reflected. Hearst Power submitted that the same approach to PST should be used for OM&A as for capital expenditures, and reiterated its proposal to remove all PST for the revenue requirement and instead record actual PST in a deferral account, to be disposed of later.

VECC submitted that depreciation expenses related to smart meters should be reduced if the capital costs of smart meters are recorded in a deferral account as advised by VECC. Hearst Power calculated depreciation in this scenario at $135,888, and provided a revenue requirement work form with this amount.[44]

Hearst Power confirmed[45] that it had not included any late payment penalty litigation costs. Hearst Power included no provision for LEAP, did not seek recovery of any cost associated with the *Green Energy Act*, and noted that it makes no charitable donations.

[42] Exhibit 4, Tab 1, Schedule 1, page 1
[43] VECC interrogatory #12
[44] IRR Appendices, Appendix 2
[45] Board staff supplemental interrogatories #26 and #30

Income and Capital Taxes

Certain data relating to PILs calculations appeared to be missing and/or variously stated in the application. The amount of PILs included in the 2010 revenue requirement was $14,479. Hearst Power filed a revised PILs model[46] in response to an interrogatory, with PILs equal to $31,038. On November 22, 2010 it filed a Revenue Requirement Work Form with PILs equal to $23,652. On December 9, 2010 it filed a further revision to the PILs model, resulting in an amount $27,260.

VECC noted that there were discrepancies remaining between the PILs calculations and the RateMaker model, and invited Hearst Power to provide an explanation. In its reply argument, Hearst Power stated that the model filed on December 9 was incorrect. It stated that problems with its PILs model had been rectified and that the effect on the revenue requirement was a reduction of $20. The submission neglected to say which of the previous calculations was to be reduced by this amount.

Board Findings

The Board accepts Hearst Power's submissions concerning the increase in its OM&A expenses, and its costs of Outside Services including the cost of supporting rate applications. The Board also approves the components of the amount of $935,399 for inclusion in the revenue requirement, except for the following issue.

The Board has noted above its acceptance of Hearst Power's proposed treatment of PST actually paid for capital spending during the first half of 2010. The Board also approves Hearst Power's proposal to remove the PST included in the 2010 OM&A and record actual PST paid in the first six months of 2010 in a deferral account for future recovery. The Board expects that Hearst Power will show in the supporting documentation for the Draft Rate Order that the PST has been effectively excluded from the test year revenue requirement.

The Board directs that depreciation on smart meters installed shall not be included in the revenue requirement, and shall continue to be recorded in account 1555. Hearst Power shall update its depreciation expense to be consistent with the Board's decision on Smart Meters, and the Board expects appropriate supporting documentation with the Draft Rate Order.

[46] Board staff interrogatory #11

The Board does not have evidence on the latest calculation of Hearst Power's PILs expense. In its reply submission, Hearst Power acknowledges that the calculation it had filed was incorrect. It suggests that the inaccuracy was quite small, but it does not make clear whether all three of the inconsistencies identified in VECC's submission were addressed or indeed whether any of them were addressed. In any event, the return on equity is affected by the Board's Decision to not allow smart meter costs in the rate base, and Hearst Power is required to include a revised PILs calculation as a result.

The Board agrees with VECC's submission that more transparency is required with respect to Hearst Power's expenses and revenues related to its affiliates. The Board expects Hearst Power to afford this matter its utmost attention, in particular by ensuring that its records show clearly all costs incurred by Hearst Power that ultimately result in revenue for Hearst Power Sales and Service.

COST OF CAPITAL AND RATE OF RETURN

In the application[47], Hearst Power applied for a 7.31% cost of capital which it expected would produce a return of $179,378[48] . The components of the Cost of Capital requested were:

- Long-term Debt: 5.87%
- Short-term Debt: 2.07%
- Equity : 9.85%

Hearst Power requested approval for a capital structure of 60% debt and 40% equity. It noted that it had a demand promissory note from the Town of Hearst, with a debt rate of 12% p.a. and with the principal variously stated as $1.8 million and $1.7 million. It explained[49] that the promissory note was for $1.8 million with a remaining balance of $1.7 million, and confirmed[50] that the promissory note is payable to the Town on demand.

Hearst Power was asked to explain why[51], in the process of responding to the preliminary interrogatories, it had increased the long-term debt rate from 5.87% in the

[47] Exhibit 5, Tabs 1-3
[48] Exhibit 5, Tab 1, Schedule 2, page 3
[49] Board staff interrogatory # 12 and Board staff supplemental interrogatory # 31
[50] VECC interrogatory #21
[51] Board staff supplemental interrogatory #9 and VECC supplemental interrogatory #40

original filing to 12.5% in the latest filing. Hearst Power responded that the rate should have been set at the Board's prescribed ceiling of 5.87%"and that this had been rectified in its updated filing.

Board staff stated that it had no issue, on the understanding the long term debt calculation is based on $1.7 million and the Board's ceiling rate of 5.87% is used for the revenue requirement VECC concurred with this position. Hearst confirmed that it is seeking approval of this cost of debt.

Board Findings

The Board approves the capital structure of Long Term Debt 56%, Short Term Debt 4%, and Equity 40%. It approves the rate of 5.87% on the Long Term Debt, 2.07% on the Short Term Debt, and 9.85% rate of return on Equity.

COST ALLOCATION AND RATE DESIGN

The following issues are addressed in this section:

- Definition of Intermediate Class
- Revenue to Cost Ratios
- Monthly Fixed and Volumetric Rates
- Transformer Ownership Allowance
- Retail Transmission Service Rates
- Low Voltage Charges
- Loss Factors
- Rate Schedules and Bill Impacts

Intermediate Class

Hearst Power has requested that its Intermediate class be defined by billing demand of 1500 kW in place of 3000 kW. The rationale is that the this billing demand is more than 10% of Hearst Power's average peak load, and that this percentage was also the rationale for the previous definition of the class. Board staff and VECC did not make submissions on this issue.[52]

[52] Exhibit 3, Tab 2, Schedule 1, p. 1

Revenue to Cost Ratios

In the application[53], Hearst Power provided its revenue to cost ratios based on 2006 data. In response to interrogatories, Hearst Power noted[54] that certain updates had not been made in accordance with the Board's guidelines and therefore revisions to the Cost Allocation Study were required. Significant changes to the previously-filed cost allocation methodology were made and updated results were filed on November 24, 2010.[55] At the same time Hearst Power submitted a different set of 2010 distribution rates along with supporting bill impact calculations.[56]

VECC noted that the revenue to cost ratios that would result, if there were a uniform percentage increase in all distribution rates to yield the requested revenue requirement, are found in the updated cost allocation study. The ratios are shown in column 2 of Table 7 below. VECC listed the revenue to cost ratios proposed by Hearst Power for 2010, as ultimately submitted in response to the supplementary round of interrogatories. These ratios are shown in column 3 of Table 7.

VECC expressed doubts about whether the revenues accurately reflected Hearst Power's revised load forecast in the distribution revenues, as well as the Applicant's proposed lower transformer ownership allowance. VECC also noted that total Miscellaneous Revenue was not equal to the updated revenue offset.

Table 7 Revenue to Cost Ratios (%)

Customer Class	Existing (Uniform Increase)	Proposed Ratios
Residential	97.79	100
GS<50 kW	104.40	99
GS > 50 kW	281.76	166
Intermediate	42.99	80
Street Light	18.21	70
Sentinel Light	62.96	70
Total	100.00	100

[53] Exhibit 7
[54] Preamble to Board staff interrogatory #14 and VECC interrogatory #23
[55] Response to Board staff supplemental interrogatory # 32; Hearst Rate Model HP-2010_20101209 worksheet O1.
[56] Responses to Board staff supplemental interrogatories, Appendix 2IR_A; Response to Board staff supplemental interrogatory #1 (RateMaker file 'Suppl IRs_20101122')

In its reply submission, Hearst Power submitted corrected distribution revenues at existing rates. With respect to the revenue offset, the Applicant reiterated that its allocation methodology was reasonable, but it acknowledged VECC's concern about the inconsistent total amount of revenue offset. It proposed to rectify the matter with its draft rate order.

With respect to rate re-balancing VECC questioned whether there was adequate reason to move the ratio for the Residential class upwards. It also submitted that it was inappropriate to move the ratio for the GS<50 kW class in the opposite direction from above 100% to below 100%. Hearst Power submitted that the bill impacts on the Residential class are below 10% and that the economy has been difficult for small business in its service area.

VECC agreed that a substantial decrease in the ratio of the GS > 50 kW class was appropriate, but questioned why it should be moved below the boundary in the Board's policy range. VECC pointed out that the Residential ratio is being increased, apparently to enable this decrease, as the Residential ratio is already within its range.

VECC agreed with the proposal to increase the ratios of the remaining classes to the lower boundary of their respective ranges. It pointed out that increases of larger magnitudes have often been phased in over several years in order to mitigate bill impacts.

Monthly Fixed and Volumetric Rates

The Applicant stated[57] that the fixed rates were established using the guidance provided in the cost allocation model for determining maximal values and minimal values. The proposed approach was to set the fixed rate no higher than the Monthly Service Charge ceiling as calculated in the updated cost allocation model. Board staff noted that the proposed Monthly Service Charge for all classes except Street Lights was within the calculated minimum/maximum range.

The fixed:variable percentage for Residential and Street Light decreased in the proposed design, relative to the existing percentage, while the fixed-rate percentage for all other classes increased – in some cases quite substantially[58]. VECC submitted a

[57] Exhibit 8, Tab 1, Schedule 1
[58] Exhibit 8, Table 8.1.1.2, and updated in response to VECC # 25(g).

table showing the proposed Monthly Service Charges, the range based on the most up-to-date 2010 cost allocation study, and also what the Monthly Service Charge would be if the existing fixed:variable percentage were to be maintained in the new rates.

Where the fixed:variable ratio is being decreased, Hearst Power's rationale was to promote conservation. VECC agreed with this proposal as it affects the Residential class. The fixed:variable ratio for the General Service classes is increased, but the fixed rate would be within the Board's guidelines. For the Intermediate class, maintaining the existing fixed:variable ratio would yield a Monthly Service Charge well below the lower boundary of the policy range. Hearst Power's proposal is a fixed:variable ratio higher than the existing ratio, but with a Monthly Service Charge remaining still below the lower boundary. VECC supported the proposal for the classes other than Residential as well.

With respect to the Intermediate class, Hearst Power clarified that it proposes to move to the lower boundary of the policy range over a period of three years. The proposed Monthly Service Charge is $320 per month. The lower boundary is $543.38 per month.[59]

Transformer Ownership Allowance

Hearst Power proposed to decrease the Transformer Ownership Allowance (TOA) from $0.60 per kW to $0.35 per kW.

Board staff noted that Hearst Power had been asked[60] to provide details of the TOA adjustment it planned to make. Hearst Power's response, reiterated in its reply submission, was that it could not provide calculations supporting the reduction of the TOA. It submitted that "Considering the age of the assets, Hearst considers an allowance of $0.35 to be fair and reasonable." Board staff submitted that this was an inadequate basis and that the Board should reject the requested TOA change.

[59] 'Run 3 2010 Cost Allocation Filing: HPL-2010', worksheet O2.
[60] Board staff supplemental interrogatory #33

Low Voltage Charges

The Applicant stated[61] that it had a 24% over-recovery on its Low Voltage (LV) charges and the current rates were reduced by this percentage to arrive at the proposed rate. It submitted a forecast 2010 cost of $77,713[62]. VECC submitted that there were inconsistencies in the information provided in support of this estimate, initially in terms of the Hydro One rates used and later in terms of the updated load forecast.

Hearst Power acknowledged VECC's argument, and submitted a revised forecast of its costs at $53,000. It pointed to an appendix which would show the details, though no appendix was found. It proposed to update the values of LV charges. [63]

Loss Factors

The total loss factor currently approved for Hearst Power is 1.0509. Hearst Power provided detailed calculations in support of the requested Loss Factors. Hearst Power originally proposed a 5-year average rate of 1.0419 based on the 2004-2008 Total loss factors. It changed its request to 1.0460 in the update filed in response to Board staff supplemental interrogatories.[64]

Board staff asked why Hearst Power's Total Loss Factor was trending upwards over time and, while not addressing the reason(s) behind the upward trend, Hearst Power stated[65] it had made an error in using the 2004-2008 average (which produced the 1.0419 value). Hearst Power stated it should instead have used the 2005-2009 average. Board staff noted that because the 2009 Total Loss Factor had suddenly increased to 1.0563 (which is in excess of the Board's 5% threshold), the new 5-year average increased to 1.0460 and is the new value for which Hearst Power requested approval. This is also the value it utilized both in the latest-filed rate schedule[66] and in its cost of power calculations. Board staff noted that, if Hearst Power had filed its application on time, the 2009 value would not have been known and the updated value would not have been an issue. It submitted that the appropriate loss factor value would be 1.0419. Board staff further submitted that Hearst Power should, before its next cost

[61] Exhibit 8, Tab 1, Schedule 3
[62] VECC interrogatory #25
[63] Hearst Power Reply Submission, p. 26.
[64] Exhibit 8, Tab 1, Schedule 4; response to Board staff supplemental interrogatory # 1, Appendix 2IR_A.
[65] Board staff supplemental interrogatory #34
[66] Appendix 2IR_A

of power rates application, undertake a study to examine its losses and file a report with the Board detailing the actions it has completed and has planned to undertake in the two years following the issuance of the report.

VECC supported the proposed loss factors.

Hearst Power argued that its proposed loss factor is less than 1.05, though the 2009 statistic is above this amount. It submitted that the requirement for a study is inappropriate.

Retail Transmission Service Rates

Hearst Power filed evidence[67] which showed that it has been over-recovering on its Retail Transmission Service Rates (RTSR). The data showed the RTSR network charge over-recovery was 3.86% and the RTSR line connection charge over-recovery was 18.08%. As a consequence, Hearst Power proposed a reduction in its RTSRs. Hearst Power is an embedded distributor and is served by Hydro One Distribution at its Retail Transmission Service Rates applicable to the Sub-transmission class. It provided two updates to its RTSR calculations, in response to an interrogatory and a supplemental interrogatory from VECC[68]. The cost calculations show a component of cost from the IESO, due to provision of service from Hydro One Transmission, as well as a component from Hydro One Distribution.

Board staff stated it did not have an issue with the ultimately-proposed RTSRs. VECC submitted that the calculation of Hearst Power's cost did not show clearly that the proposal was based on Hydro One's 2010 rates and Hearst Power's 2009 volumes. Hearst Power submitted in reply that it had used the 2010 rates together with 24 months of historic data, and that this provided an appropriate methodology that has been used by other utilities.

[67] Exhibit 8, Tab 1, Schedule 2
[68] VECC interrogatories #7 and #27; VECC supplemental interrogatory #49

Rate Schedules and Bill Impacts

The Applicant provided a table of the bill impacts for Residential customers using 800 kWh per month. While delivery charges were shown to increase by 20.82% ($3.66 per month), the total bill averaged over winter and summer increased by 2.73% ($2.33 per month).

In its application[69], Hearst Power purported to reconcile the proposed rates but no actual comparison of the expected revenue and the revenue requirement was provided. It later provided a reconciliation[70] of its proposed rates and forecast volumes in response to interrogatories. While the reconciliation showed that the calculated and allocated values were very close, Board staff observed that the variable rates used for most of the customer classes in the calculations did not match those in the latest-filed rate schedule[71]. Updated bill impact calculations were provided by Hearst Power in the RateMaker model filed on December 9, 2010. The model shows bill impacts for one customer per class, except for the Residential class with two examples.

The total bill impacts calculated in Hearst Power's RateMaker model are shown in Table 8. The impacts include the effect of rebates of Deferral and Variance account balances per Hearst Power's application.

Table 8 Bill Impacts

Rate Class	Delivery Bill Impact	Total Bill Impact
Residential *	25.1 %	6.1 %
GS<50 kW	21.8 %	3.9%
GS>50 kW	(14.5 %)	(2.9 %) **
Intermediate	(1.4 %)	(0.6 %)
Sentinel Lights	25.6 %	7.2 %

* Winter rates, 1000 kWh per month

** calculation provided by Board staff

Board staff submitted that in order to give the Board a degree of confidence in the rates being proposed, Hearst Power should provide a reconciliation utilizing the latest-filed load forecast[72] and the updated proposed rate schedule.

[69] Exhibit 8, Tab 1, Schedule 5, and Appendix 6, submitted May 25, 2010. Updated November 22, 2010, in response to Board staff supplemental interrogatory # 1, 'EDR_SUPPL IRs_20101122'
[70] Board staff supplemental interrogatory #18 and VECC supplemental interrogatory #37
[71] Appendix 2IR_A
[72] Appendix 2IR_F

VECC noted that the updated record did not include a calculation of the bill impact on Street Lights. Hearst Power proposed to produce this information with its draft rate order.

Board Findings

The Board finds that the definition of the Intermediate class with billing demand above 1500 kW is appropriate, as proposed by Hearst Power.

In the following directions regarding revenue to cost ratios and rate re-balancing, the Board accepts as the starting point the values in Table 7 above. The Board agrees with VECC that Hearst Power has not established an adequate basis for increasing the revenue to cost ratio of the Residential class above its current amount, and directs Hearst Power to maintain the ratio at 98%. The Board also agrees with VECC concerning the reduction in the revenue to cost ratio for the General Service < 50 kW class, and directs that the ratio be moved to100% rather than below. The Board accepts the applicant's proposed revenue to cost ratios Sentinel Lighting, with a ratio of 70%.

With respect to the Intermediate class the Board notes that the revenue to cost ratio for the Intermediate class was calculated at 78.60% in Hearst's application (2006 results, after correction for the Transformer Ownership Allowance)[73]. The 2010 ratio was subsequently calculated at 111.16%, based on a uniform percentage increase in rates to satisfy the total revenue requirement.[74] Hearst Power confirmed in response to Board staff supplemental interrogatory #32 that the re-filed rates were based on the latter cost allocation results. However, Hearst Power filed another cost allocation study, in which the Intermediate class revenue to cost ratio would be 42.99%[75] after a uniform percentage adjustment. The rates proposed for the Intermediate class are consistent with an increase of the ratio from a starting point of 43%, and not consistent with a starting point of 111%. The Board approves a revenue to cost ratio for the Intermediate class of 80% as proposed by Hearst Power, on the understanding that the ratio of the Intermediate class is 43% and all ratios before re-balancing are those presented in Table 7 above.

[73] Application, Table 7.1.1.1
[74] Appendix BS-K of Responses to VECC interrogatories (p. 12)
[75] Response to Board staff supplemental interrogatory # 1, 'Rate Model_HPL-2010' filed December 9, 2010.

The Board finds that the changes proposed for Street Lights shall be phased in over two years. The revenue to cost ratio for Street Lights shall be 50% for 2010 rates, continue at 50% for 2011 rates, and shall be increased to 70% with the 2012 rates.

The Board understands that the outcome of the ratios ordered in this and the previous paragraphs may result in a higher or lower ratio for the General Service > 50 kW class than was proposed by the Applicant. For 2010 and 2011, Hearst Power shall demonstrate what ratio is achieved as a net outcome of the re-balancing of the other classes. With 2012 rates, Hearst Power will achieve a revenue to cost ratio of no higher than 180% for the General Service > 50 kW class, and if necessary to attain this ratio it may raise the Residential ratio toward 100%.

Hearst Power is directed to include documentation with its Draft Rate Order to support its revenue to cost ratios and the resulting distribution rates and revenues for all classes. It will show the revenue to cost ratios in which revenues are compared to the results of Hearst Power's most up-to-date cost allocation study.

The Board accepts Hearst Power's rate design with respect to fixed and variable proportions for each class. In particular, it accepts the proposal to increase the Monthly Service Charge to the Intermediate class to ultimately be equal to $543.38 plus IRM increases, within three years following this rate re-basing, and it recognizes that the volumetric rate to this class will likely increase by a lower percentage amount than the fixed charge while that adjustment is being made.

The Board does not accept Hearst Power's proposal that the Transformer Ownership Allowance should be reduced to $0.35 per kW. The Board notes that the cost allocation study submitted by Hearst Power shows the cost of line transformers to the General Service > 50 kW class is $0.45 per kW. The study does not show a corresponding number for the Intermediate class, perhaps because the distributor provides no transformers to the customers in that class. The Board directs Hearst Power to set the monthly Transformer Ownership Allowance at $0.45 per kW, on the basis that this is the outcome of the updated cost allocation study filed in support of this Application.[76]

The Board accepts Hearst Power's revised forecast of its Low Voltage cost at $53,000 per year. It expects that the documentation supporting the Draft Rate Order will show

[76] Response to Board staff supplemental interrogatory # 1 'Rate Model_HPL-2010' filed December 9, 2010, worksheet O3.1 'Line Tran Unit Cost'.

clearly that this cost has been used in the calculation of the Low Voltage Service Rates in the tariff.

The Board notes that Hearst Power is requesting a substantial decrease in its Total Loss Factor. The calculation includes one year of high actual losses that is hopefully not an indication of future losses. The Board will accept the proposed Total Loss Factor of 1.0460 for secondary-metered customers and the corresponding factor for primary-metered customers.

With respect to Retail Transmission Service Rates, the Board notes that new Uniform Transmission Service Rates have been approved by the Board, and that the IESO will charge these rates to Hearst Power in 2011 which will affect the relevant portion of the wholesale cost,. Given the effective date of Hearst Power's rates, it is evident that an update of the calculation submitted by the Applicant should be done. Hearst Power's proposed Retail Transmission Service Rates are approved, with this adjustment. The revised calculation is to be documented with the Draft Rate Order.

The Board notes that it would have been helpful if Hearst Power's reply submission had included an indication of the bill impact on the Street Light class, which VECC had pointed out was missing from the updated evidence filed on December 9, 2010. In the absence of this information, the Board has only the impact calculation filed with the original application, which showed a 57% impact.[77] Given that the Board has specified a revenue to cost ratio of 50% in 2010 and 2011, the Board expects that the bill impact on Street Lights will be lower than 57%.

DEFERRAL AND VARIANCE ACCOUNTS

General Rate Rider

Hearst Power identified[78] the deferral accounts it proposed to dispose of over a four year period and those accounts for which it proposed to wait for the Board's direction. Board staff noted there was a lack of clarity in the application regarding the nature of some of the account balances that the Applicant proposed to clear; and that the calculation of the proposed four-year rate riders was not transparent.

[77] Appendix 6, p. 836 of 837.
[78] Exhibit 9, Tab 1, Schedule 3

Hearst Power subsequently provided a detailed explanation[79] regarding how it proposed to clear its deferral and variance accounts. It also stated that it was not opposed to Board staff's suggestion regarding the establishment of a variance account to capture the reduction in OM&A and capital expenditures due to HST, though its preference would be to use the method proposed by Renfrew Hydro[80]; i.e. the establishment of a variance account to track the Input Tax Credits ("ITCs") on revenue requirement items that were previously subject to PST).

Board staff submitted it had no issue with Hearst Power's proposed clearance of its deferral and variance accounts and the calculation method of its proposed rate riders.

Hearst Power calculated[81] the applicable rate rider for the Global Adjustment and verified that it would only apply prospectively to non-RPP customers, in the non-MUSH sector ("Municipalities, Universities, Schools and Hospitals").

Hearst Power provided a calculation of its proposed rate riders, based on disposition of accounts 1508, 1518, 1525,1548, 1550, 1565, 1566, RSVA accounts, and 1598, in response to a supplementary interrogatory.[82] The inputs to the calculation do not include a balance for account 1598. VECC submitted that its only concern was the inclusion of accounts 1570 and 1571 in the list of accounts for disposition. These accounts are for pre-market and transition costs which require a prudence review prior to disposition. Hearst Power replied that the inclusion of the accounts resulted from a misunderstanding and that it did not seek disposition at this time.

VECC also expressed its reservations about the length of the proposed disposition over four years, and suggested that a shorter period should be considered in the interests of inter-generational equity. Hearst Power replied that its objective was to maintain rate stability throughout the period until its next re-basing.

Establish a Deferral Account for Unforeseen Considerations

In its application[83], Hearst Power requested approval "To establish a deferral account to be used for reasonable costs not allowed by the Board because of considerations not

[79] Board staff supplemental interrogatory #37
[80] EB-2009-0146, Exhibit 9, Tab 1, Schedule 1, pp. 2-3
[81] Board staff supplemental interrogatory #40
[82] The combined balance is approximately $35,000. Reference: Appendix 2IR_I, worksheet C6.
[83] Exhibit 1, Tab 1, Schedule 4, Page 2, List of Specific Approvals Requested, item #12

foreseen by the applicant".
Hearst Power[84] was asked to provide further details of its request and, in particular, to identify what types of circumstances the account is meant to address and how these circumstances would differ from those applicable for a Z-factor adjustment. Board staff and VECC submitted that the Board had already provided adequate mechanisms to handle contingencies and that the Board should not approve the additional deferral account.

Smart Meter Riders

In its application[85], Hearst Power stated that it began installing smart meters in March 2009. By 2009 year end, 86% of the meters were installed and by 2010 year end, 100% (2,751 meters) were forecasted to be installed. In its application, Hearst Power requested approval to discontinue the smart meter $1.00 per month funding adder for all metered customers.

Board Findings

Hearst Power requested a deferral account to record the cost of unforeseen events. The Board agrees with VECC and Board staff that the account is not necessary. In Section 2.6 of the *Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors,* dated July 14, 2008 the Board noted that Z-factors are intended to provide for unforeseen events outside of management's control. The Board does not approve Hearst Power's request for a new deferral account for unforeseen events because it would be redundant.

As noted earlier in this Decision, the Board will approve the inclusion of actual PST paid in the first six months of 2010 in a deferral account for future recovery.

The Board has declined Hearst Power's request to transfer smart meter balances to its rate base. The Board directs that Hearst Power continue to track revenues received from the smart meter funding adder, and actual costs incurred, in the established smart meter related variance accounts, for review and disposition in a subsequent application. The Board notes that the schedule for smart meters implementation indicates that installation should be completed or close to completion by the date of this Decision, and

[84] VECC interrogatory #2
[85] Exhibit 9, Tab 1, Schedule 4

that Hearst Power will be in a position to file a stand-alone application for the disposition of balances in the smart meter deferral and variance accounts (1555 and 1556) and the establishment of smart meter incremental revenue requirement rate rider. The rate rider would proxy the revenue requirement going forward for all smart meters installed, to be in effect until Hearst Power's next rebasing application. The Board reminds Hearst Power that such an application must meet the requirements contained in Guideline G-2008-0002 in order to enable the Board to conduct a prudence review.

In the meantime, the Board will approve a smart meter funding adder of $2.50 per metered customer per month. This funding adder will replace the existing smart meter funding adder of $1.00 per metered customer per month. The Board will approve this smart meter funding adder until April 30, 2012 or until such time that the Board approves the disposition of balances in variance accounts 1555 and 1556 and the establishment of smart meter incremental revenue requirement rate rider.

In approving this smart meter funding adder, the Board has not made any finding on the prudence of the proposed smart meter activities, including any costs for smart meters or advanced metering infrastructure whose functionality exceeds the minimum functionality adopted in O. Reg. 425/06, or costs associated with functions for which the Smart Metering Entity has the exclusive authority to carry out pursuant to O. Reg. 393/07. Such costs will be considered at the time that Hearst Power applies for the recovery of these costs.

The Board approves rate riders designed to dispose of the accounts in Hearst Power's revised list, which it understands no longer includes accounts 1570 and 1571. The Board expects that Hearst Power will include an explanation of account 1598, will show clearly what the balance is in that account, and will show how the rate riders are calculated for each rate class whose rate riders are affected by it. If the inclusion of account 1598 has a material effect on the rate riders, Hearst Power shall include two calculations, one with it included and one with it excluded.

The Board finds that the recovery period of four years is longer than necessary. It will approve rate riders designed to recover the balance over a 27-month period, beginning from the effective date of this Decision and continuing through the 2011 and 2012 rate years, and ending on April 30, 2013.

IMPLEMENTATION OF RATES

Earlier in this Decision, the Board approved February 1, 2011 as the effective date for the rate changes. Given the time that is required for the process leading to the issuance of a rate order and the need for Hearst Power to implement the new rates into their billing systems, it may not be possible to implement the new rates until April 1, 2011. The foregone distribution revenue from February 1, 2011 to March 31, 2011 shall be recovered through a rate rider in effect from April 1, 2011 to April 30, 2012. If the implementation date of April 1, 2011 is not feasible, Hearst Power shall provide the intended implementation date in its Draft Rate Order; however this date should be as soon as possible.

The Board's findings outlined in this Decision are to be reflected in a Draft Rate Order. The Board directs Hearst Power to file detailed supporting material, including an updated PILs calculation, updated Revenue Requirement Work Form, allocation of the approved revenue requirement to the classes, determination of the final rates and rate riders, and bill impacts.

A Rate Order will be issued after the steps set out below are completed.

THE BOARD DIRECTS THAT:

1. Hearst Power shall file with the Board, and shall also forward to VECC, a Draft Rate Order attaching a proposed Tariff of Rates and Charges and other filings reflecting the Board's findings in this Decision within 14 days of the date of this Decision.

2. Board staff and VECC shall file any comments on the Draft Rate order with the Board and forward them to Hearst Power within 7 days of the date of filing of the Draft Rate Order.

3. Hearst Power shall file with the Board and forward to VECC, responses to any comments on its Draft Rate Order within 7 days of the date of receipt of intervenor submissions.

COST AWARDS

The Board may grant cost awards to eligible stakeholders pursuant to its authority under section 30 of the *Ontario Energy Board Act, 1998*. The Board will determine cost awards in accordance with its Practice Direction on Cost Awards. When determining the amounts of the cost awards, the Board will apply the principles set out in section 5 of the Board's Practice Direction on Cost Awards. The maximal hourly rate set out in the Board's Cost Awards Tariff will also be applied.

VECC submitted that its participation in this proceeding had been focused and responsible, and accordingly requested a 100% award of its reasonably-incurred fees and disbursements.

A cost awards decision will be issued after the following steps have been completed.

1. VECC shall file with the Board, and forward to Hearst Power, its cost claims within 10 days from the date of the Rate Order

2. Hearst Power shall file with the Board and forward to VECC, any objections to the claimed costs within 17 days from the date of the Rate Order

3. VECC shall file with the Board and forward to Hearst Power any responses to any objections for cost claims within 24 days of the date of the Rate Order.

Hearst Power shall pay the Board's costs incidental to this proceeding.

All filings to the Board must quote the file number, EB-2009-0266, be made through the Board's web portal at www.errr.oeb.gov.on.ca, and consist of two paper copies and one electronic copy in searchable / unrestricted PDF format. Filings must clearly state the sender's name, postal address and telephone number, fax number and email address. Please use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at www.oeb.gov.on.ca. If the web portal is not available parties may email documents to the address below. Those who do not have internet access are required to submit all filings on a CD or diskette in PDF format, along with two paper copies. Those who do not have computer access are required to file 7 paper copies. All communications should be directed to the attention of the Board Secretary at the address below, and be received no later than 4:45 p.m. on the required date.

ADDRESS

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4
Attention: Board Secretary
E-mail: Boardsec@oeb.gov.on.ca
Tel: 1-888-632-6273 (toll free)
Fax: 416-440-7656

DATED at Toronto, February 15, 2011

ONTARIO ENERGY BOARD

Original Signed By

____
Marika Hare
Presiding Member

Original Signed By

____
Ken Quesnelle
Member