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BY EMAIL

April 15, 2011

Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: Board Staff Interrogatories for Brant County Power Inc.
EB-2010-0125

Further to the Board's Procedural Order No. 5, dated April 12, 2011, please find attached Board staff's submission on the cost of service rates application filed by Brant County Power Inc. on November 5, 2010.

Please forward the attached to Brant County Power Inc. and all intervenors in this proceeding.

Yours truly,

Original signed by

Christie Clark
Case Manager

Enclosure

Board Staff Submission

Brant County Power Inc.
EB-2010-0125

Procedural Order No. 5, in Brant County Power Inc.'s ("Brant County") EB-2010-0125 rate application directed parties wishing to file a submission to do so by April 15, 2011. The following is Board staff's submission.

Introduction

Brant County filed a cost of service application with the Ontario Energy Board (the "Board"), on November 5, 2010 for new rates effective May 1, 2011. On March 22nd and 23rd, 2011 Brant County and two of the intervenors, Energy Probe Research Foundation and the Vulnerable Energy Consumers Coalition (the two collectively known as the "Two Intervenors") convened for the purposes of negotiating a settlement agreement. The third intervenor, Brantford Power Inc., did not participate. On April 8, 2011, Brant County filed a proposed Settlement Agreement (the "Agreement") in which all issues were settled with the exception of Brant County's proposal to adjust the revenue-to-cost ratios for the Residential and three General Service customer rate classes.

Positions of the Parties

The Agreed Upon Revenue-to-Cost Ratios

The Parties agreed to increase the revenue-to-cost ratios for the Street Lighting and Sentinel Lighting to the bottom of their respective revenue-to-cost ratio ranges, as set by the Board in its report *Application of Cost Allocation for Electricity Distributors* (the "Report").[1] The following table shows the starting revenue-to-cost ratios before any adjustments, the agreed upon proposed revenue-to-cost ratios, and the Board approved ranges:

	Start Position	Proposal	Board Ranges
Street Lighting	10.8%	70.0%	70% - 120%
Sentinel Lighting	32.9%	70.0%	70% - 120%

The additional revenue from these customer rate classes would be used to reduce the revenue-to-cost ratio for the GS 50 - 4,999 kW rate class.

The Disputed Revenue-to-Cost Ratios

Brant County is proposing to adjust the revenue-to-cost ratio to 100% for all other rate classes except for the GS 50 – 4,999 kW rate class.

[1] EB-2007-0667 Report of the Board: *Application of Cost Allocation for Electricity Distributors*

In the Agreement, the Two Intervenors' proposed that no revenue-to-cost ratio adjustments be made to the Residential and three General Service rate classes, for they are currently within the Board-approved ranges.

The following table compares the positions of Brant County and the Two Intervenors, and provides the Board's approved revenue-to-cost ratio ranges:[2]

	Start Position	Brant County	Intervenors	Board Ranges
Residential	92.38%	100%	92.38%	85% - 115%
GS < 50 kW	102.77%	100%	102.77%	80% - 120%
GS 50 - 4,999 kW	142.14%	109.15%	124.62%	80% - 180%
USL	117.57%	100%	117.57%	80% - 120%

The Issue: Revenue-to-Cost Ratios

The revenue-to-cost ratio is an expression of the ratio between the revenue that is forecasted to be recovered from a rate class to the forecasted costs that are allocated to that class. It is one of the measures regulators consider in assessing just and reasonable rates. Key to the revenue-to-cost ratio is the cost allocation methodology.

Accuracy of the Cost Allocations

Board staff submits that the allocation of the revenue requirement is an estimate of the forecast cost to serve each rate class as the cost allocation methodology requires the exercise of judgment and the use of estimates and forecast data in establishing cost causality. Cost allocation models are also complex, requiring time to develop experience with them. The Board recognized these challenges in its Report:

> "The Board is cognizant of factors that currently limit or otherwise affect the ability or desirability of moving immediately to a cost allocation framework that might, from a theoretical perspective, be considered the ideal. These influencing factors include data quality issues and limited modelling experience, and are discussed in greater detail in section 2.3 of this Report. The Board also recognizes however, that cost allocation is, by its very nature, a matter that calls for the exercise of some judgment, both in terms of the cost allocation methodology itself and in terms of how and where cost allocation principles fit within the broader spectrum of rate setting principles that apply to – and the objectives sought to be achieved in – the setting of utility rates. The existence of the influencing factors does not outweigh the merit in moving forward on cost allocation. Rather, the Board considers that it is both important and appropriate to implement cost allocation policies at this time, and believes that the policies set out in this Report are directionally sound. With better quality data, greater experience with cost allocation modeling and

[2] ibid

> further developments in relation to other rate design issues, the policies will be refined as required."[3]

Section 2.3 of the Report addressed factors that the Board took into account in developing its policy on revenue-to-cost ratios. These factors were:

- **Quality of the data:** The Board felt that there was room for improvements in accounting and load data;
- **Limited modelling experience:** The Board recognized that the model is complex and that as analysts become more familiar with the model and the relationships between operating statistics and accounting data, results will become more reliable;
- **Status of current rate classes:** The Board pointed out that the introduction of smart metering may lead to new ways of looking at rate classes and structures; and
- **Managing the movement of rates closer to the allocated costs:** The Board found it appropriate to avoid premature movement of rates in case future changes to the model leads to subsequent counter directional changes.

Therefore, the Board found it appropriate, as a directionally sound approach, to set ranges for revenue-to-cost ratios.

The Board recently held a review of specific cost allocation issues with the cost allocation model and published its findings; Report of the Board: *Review of Electricity Distribution Cost Allocation Policy* (the "Review").[4] One issue in the Review was to consider narrowing the three widest revenue-to-cost ratio ranges. Board staff notes that the Review did not contemplate to move away from using target ranges for revenue-to-cost ratios to set rates.

While the Board in the Review narrowed the revenue-to-cost ratio ranges for the Sentinel Lighting rate class (from 70% - 120% to a range of 80% - 120%) and the GS 50 – 4,999 kW rate class (from 80% - 180% to 80% - 120%), the Board held the range for the Street Lighting rate class (70% - 120%) The Board found that, as there is a planned separate consultation on the terminology and improvement of cost allocation methods for the Street Lighting rate class, the range for this class should not change at this time.

Board staff notes that when changes are made to the allocation of costs, such as the allocation of costs to the Street Lighting rate class, all other classes are affected. That is because the model is a fully allocated cost model. As such all costs are fully distributed to the classes. In other words, it is a zero sum game: If the costs to one class go down, then other classes see their costs increase to offset the reduction to that one class.

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[3] Ibid p. 2
[4] EB-2010-0219 Report of the Board: *Review of Electricity Distribution Cost Allocation Policy*

As a result of the Review, and starting with 2012 cost of service applications, the Board has confirmed that the allocation model will be modified to accommodate, among other things, the following refinements:

- Allocation of miscellaneous revenues;
- Allocation to the Unmetered Scattered Load rate class; and
- Allocation factor weightings for services and billing costs.

As a result of these refinements, the costs allocated to Brant County's rate classes will change.

Using Boundaries

Board staff submits that the Board is eminently aware of the limitations of the cost allocation model. The Board has said:

> "The Board has concluded that an incremental approach is appropriate in light of the influencing factors identified below, and that a range approach is preferable to implementation of a specific revenue-to-cost ratio. Influencing factors aside, a revenue-to-cost ratio of one may not be achievable or desirable for other reasons (for example, to accommodate different rate design objectives). In addition, as a practical matter there may be little difference between a revenue-to-cost ratio of near one and the theoretical ideal of one."[5]

The Board has set boundaries that can be viewed as statistical bounds, due to the variations that occur in estimates or modelling assumptions. Board staff submits that statistically, all ratios in a range have equal probability of being the true ratio. That is, for the residential class as an example, a revenue-to-cost ratio of 85% statistically has the same probability of being the true value as a revenue-to-cost ratio of 100%, or 115% due to the limitations addressed in section 2.3 of the Report. While it is convenient to state that 100% is the middle and should be used, there is no statistically valid reason to do so. The Board recognized this fact when it has set boundaries and said; "as a practical matter there may be little difference between a revenue-to-cost ratio of near one and the theoretical ideal of one."

Board staff acknowledges that in the Review, the Board stated:

> "The Board's policy remains that distributors should endeavour to move their revenue-to-cost ratios closer to one if this is supported by improved cost allocations."[6]

Board staff submits that Brant County has not provided evidence to support improved cost allocations. Therefore, there is no justification to move to a revenue-to-cost ratio of 100% at this time.

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[5] EB-2007-0667 Report of the Board: *Application of Cost Allocation for Electricity Distributors*, p. 4
[6] EB-2010-0219 Report of the Board: *Review of Electricity Distribution Cost Allocation Policy*, p.36

Future Rate Impacts

As Brant County pointed out in its submission, principles other than rate impacts and rate stability should also be considered.

Board staff submits that movement in one direction of rates now with the current cost allocation model could be reversed in the next version of the cost allocation model, which would be based on the Review. In other words, Board staff is not just concerned about rate impacts, but also about a future yo-yo effect.

Conclusion

Board staff concludes that there is no reason to move classes to a revenue-to-cost ratio of 100% at this time. Board staff is concerned about a possible yo-yo effect in the future arising from improving the cost allocation model's accuracy through implementing the Review.

While it is true that in the past the Board has approved some applicants' requests to move closer to 100%, those findings were made before the Board issued its Review.

As set out above, given extenuating circumstances the Board has indicated that "a range approach is preferable" and, due to the setting of ranges "as a practical matter there may be little difference between a revenue-to-cost ratio of near one and the theoretical ideal of one. " Board staff submits that the ranges from the Report are the correct ranges to use for Brant County in this application, and that no further movement to 100% is needed.