Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2011 COS APPLICATION FOR ELECTRICITY DISTRIBUTION RATES

EFFECTIVE MAY 1, 2011

Parry Sound Power Corporation

EB-2010-0140

April 26, 2011

INTRODUCTION

Parry Sound Power Corporation ("Parry Sound Power" or the "Applicant") is a licensed electricity distributor serving approximately 3,300 customers in the Town of Parry Sound, Ontario. Parry Sound Power filed its 2011 electricity distribution rates rebasing application (the "application") on October 15, 2010.

Parry Sound Power requested approval of its proposed distribution rates and other charges effective May 1, 2011. The application was based on a future test year cost of service methodology. Parry Sound Power's distribution rates were set on a Cost of Service basis in 2006 and were set in the subsequent years under the Incentive Rate Mechanism ("IRM").

The Board issued the Letter of Direction and Notice of Application (for publication) on November 4, 2010. Parry Sound Power filed its Affidavit of Publication with the Board on November 15, 2010. The Vulnerable Energy Consumers' Coalition ("VECC") was granted intervenor status and eligibility for a cost award. Parry Sound Power did not receive any letters of comment as a result of the publication of the Notice.[1]

This submission reflects observations and concerns which arise from Board staff's review of the pre-filed evidence and interrogatory responses made by Parry Sound Power, and are intended to assist the Board in evaluating Parry Sound Power's application and in setting just and reasonable rates.

THE APPLICATION

In its pre-filed evidence, Parry Sound Power proposed a 2011 service revenue requirement of $2,714,943 (or a base revenue requirement of $2,613,957[2]). This compares to the 2006 RP-2005-0020/EB-2005-0404 Decision and Order where the Board approved Parry Sound Power's distribution rates to recover a service revenue requirement of $2,036,534 (including an amount of $104,274 for regulatory assets).

A summary of Parry Sound Power's proposed revenue requirement is presented in the table below.[3] The 2011 revenue deficiency, calculated using 2010 approved rates, that Parry Sound Power seeks to recover through the rates proposed is $791,616.

One significant impact in the bridge and test years is Parry Sound Power's restructuring into a stand-alone distribution utility after the Board denied Parry Sound Power its requested exemptions from the Affiliate Relationships Code (ARC) in 2009 (EB-2009-0133, decision dated November 12, 2009). This has resulted in additional capital and operating expenditures which are discussed below.

1 Response to Board Staff IR #1
2 Base revenue requirement is the service revenue requirement less Other Revenue of $100,986.
3 There may be immaterial differences in the numbers quoted in this submission due to rounding.

2011 Revenue Requirement Components Parry Sound Power	
OM&A	$ 1,795,417
Amortization/Depreciation	$ 389,525
Property Taxes	$ -
Capital Taxes	$ -
Income Taxes (grossed up)	$ 47,696
Other Expenses	$ -
Return - interest	$ 247,203
Return - ROE	$ 235,104
Service Revenue Requirement	$ 2,714,945
Revenue Offsets	$ 100,986
Base Revenue Requirement	$ 2,613,959

Parry Sound Power calculated the following monthly bill impacts if the application is approved as filed.[4]

Parry Sound Power - Delivery Charge Impact -increase in delivery costs over current rates- *			Total Bill	
			$ Impact	**% Impact**
	$ impact	**% impact**		
Residential @ 800 kWh	$ 16.50	39.2%	$ 20.28	16.1%
GS < 50kW @ 2000kWh	$ 29.30	37.4%	$ 37.20	13.1%
GS > 50kW @ 30,000kWh, 100kW	-$ 75.07	-6.6%	-$ 25.70	-0.6%
Streetlighting 1061 connections	$2,199.37	97.3%	$2,626.02	28.4%
Unmetered Scattered Load 272 kWh	$ 55.39	193.3%	$ 63.15	107.4%
* includes monthly charge, variable charge, adders, riders and retail Tx				

In its April 13, 2011 Argument-in-Chief, Parry Sound Power identified a number of areas where a change to the amounts presented in the pre-filed evidence was required. This included changes to OM&A, capital, a load forecast update and a proposal to recover Deferral and Variance Accounts over 4 years to mitigate total

[4] Response to Board Staff IR#2

bill impacts (reduced from 16.1% to 9.7% for a Residential customer using 800 kWh per month). These changes are addressed in more detail under the specified sections below.

In addition, Parry Sound Power also requested a number of other approvals:

- A change in its rate year, from the May 1 to April 30 period to a calendar year period (January 1 to December 31), starting January 1, 2012.
- A change in Loss Factors.
- A change in Capital Structure.
- A proposal to dispose of its Deferral and Variance account balances.
- An LRAM/SSM recovery.

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

In response to Board Staff IR # 44, Parry Sound Power confirmed that the revenue requirement amount proposed for 2011 was based on Canadian General Accepted Accounting Principles (CGAAP) and that it will not be presenting financial statements under IFRS rules until the financial statements are prepared for the fiscal year ending December 31, 2012.

In response to Board Staff IR #45 Parry Sound Power also confirmed that no amounts were included in the proposed revenue requirement for IFRS transition costs and indicated that transition costs are recorded in a sub account of 1508 (Other Regulatory Assets – IFRS Transition Costs).

Board staff has no concerns regarding the status of IFRS matters as described by Parry Sound Power. Staff expects the Board to issue guidance later this year to distributors with respect to addressing IFRS issues during IRM years.

ALIGNMENT OF RATE YEAR TO CALENDAR YEAR

Parry Sound Power applied for distribution rates to be effective as of May, 1, 2011. In its Argument-in-Chief, Parry Sound Power requested that rates be made interim as of May 1, 2011. On April 25, 2011 the Board issued an Order granting this request.

As part of this application, Parry Sound Power also requested that starting in January 2012, its rate year be aligned with its fiscal year. In doing so, Parry Sound Power relied on the Board's April 15, 2010 letter regarding these matters. Parry Sound Power's pre-filed evidence provided responses[5] to the 5 issues raised by the Board in Appendix B of the April 15, 2010 letter. Board staff has reviewed the evidence presented and has no concerns regarding this request.

[5] Exhibit 1/Tab 1/Schedule 4

LOAD FORECAST

Parry Sound Power's test year load forecast totals 88,903,303 kWh and 100,148 kW. This represents a slight increase in system wide consumption of 0.1% from 2009 actual. The proposed and actual volumes by customer class are set out in the table below.[6]

Parry Sound Power
Actual and Forecast Load, 2006 - 2011

PARRY SOUND POWER LOAD VOLUMES	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
Residential kWh	33,237,936	33,976,663	34,709,666	34,307,486	33,832,405	33,427,924
GS< 50 kW kWh	16,473,586	16,945,672	17,104,386	16,323,230	16,748,564	16,733,379
GS >50 kW kWh	35,380,706	37,168,365	36,469,790	37,202,366	36,171,050	37,802,659
GS >50 kW* kW	88,798	90,489	89,597	94,156	96,048	96,631
Street lighting kWh	867,846	867,846	870,724	867,846	867,846	867,846
Street lighting kW	2,424	2,424	2,424	2,424	2,422	2,421
Sentinel Lighting kWh	15,986	16,006	15,972	12,745	12,745	12,745
Sentinel Lighting kW	41	41	47	39	38	36
USL kWh	129,531	118,251	59,578	59,286	59,000	58,750
Total kWh	**86,105,591**	**89,092,803**	**89,230,116**	**88,772,959**	**87,691,610**	**88,903,303**
% change	-3.4%	3.5%	0.2%	-0.5%	-1.2%	1.4%
Total kW	**91,263**	**92,954**	**92,068**	**96,619**	**98,508**	**99,088**
% change	-0.4%	1.9%	-1.0%	4.9%	2.0%	0.6%

Note: * GS>50 kW 2011 value updated as per Response to VECC IR # 3j.

Load Forecasting - Methodology

In its pre-filed evidence[7], Parry Sound Power indicated that it utilized the same regression analysis used by a number of other distributors to forecast weather normalized loads.

Parry Sound Power calculates the kWhs consumed for the Residential, GS<50kW, and GS>50kW customer classes on a pro-rated basis. The regression analysis relates the other monthly explanatory variables such as heating and cooling degree days which occur in the same month. The result of the regression analysis

[6] Exhibit 3/Tab 2/Schedule 1, page 6
[7] Exhibit 3/Tab2/Schedule 1

produces an equation that predicts consumption based on the explanatory variables. This prediction model is then used as the basis to forecast the total level of weather normalized consumption for the bridge and test year.

Parry Sound Power's weather normalized load forecast is developed based on a multifactor regression model that incorporates historical load, weather, and economic data.

The forecast of customers by rate class is determined using a geometric mean analysis except for the Street Lighting, Sentinel Lighting, and Unmetered Scattered Load classes where Parry Sound Power is not forecasting any changes to the current number of customers through the Test year.

The regression analysis model has determined the main drivers of year-over-year changes in Parry Sound Power's load growth as economic, weather, and "calendar" factors. Economic growth is captured in the model using an index of economic output, the Ontario Real Gross Domestic Product ("GDP"). Weather impacts are apparent in both the winter heating and summer cooling seasons and both Heating Degree Days and Cooling Degree Days are modeled. "Calendar" factors are described as the energy use that changes due to particular months. The modeling of purchased energy uses the time trend in the month and a "flag" variable to capture the typically lower usage in the spring and fall months.

The forecast was also adjusted for CDM targets set for Parry Sound Power and the anticipated decline in consumption.

Parry Sound Power provided a record of the accuracy of the regression model.[8] Between 2004 and 2009, the variance between predicted and actual volumes was:

- 1.2% or less for the Residential class from 2004 to 2009
- 0.7% or less for the GS<50 kW class from 2004 to 2007, a -1.6% variance in 2008, then followed by a 2.4% variance in 2009.
- 4.4% in 2004; followed by -3.8% in 2005, followed by less than 1.0% from 2006 to 2009 in the GS>50kW class.

In response to VECC IR #40, Parry Sound Power provided 2010 actual consumption for these three classes which revealed more significant differences: The Residential variance grew to 5.4%, the GS<50kW grew to 7.5% and the GS>50 kW grew to 2.5%.

Parry Sound Power also indicated that the forecast consumption the Street Lights, Sentinel Lights, and Unmetered Scattered Load classes was estimated using logic and intuition based on a review of the historical usage patterns for those classes. Although no change in consumption is forecast for both Street Lights and Sentinel

[8] Exhibit 3/Tab 2/Schedule 1/page 11

Lights, a slight reduction is forecast for the USL class consistent with the trend experienced in 2008 and 2009.

Board staff notes, that in its Argument-in-Chief, Parry Sound Power indicated that it would amend its weather regression load model using 2010 actual data. Board staff supports this change in light of the differences in the actual 2010 results compared to the 2010 forecast in the pre-filed eveidence.

CDM Target

Parry Sound Power's initial pre-filed evidence included the calculation of the CDM target. Board staff notes that the 2011-14 Net Cumulative Energy Savings Target set for Parry Sound Power in the EB-2010-0215/0216 Decision and Order, dated November 12, 2010, is 4.16 GWh. The 2014 Annual Peak Demand Saving Target is 0.740 MW.

Parry Sound Power has used a target of 1.0 GWh as its overall 2011 target Parry Sound Power has simply divided its 4.0 GWh target equally by 4 years to arrive at the impact in its load forecast. This total impact is 1.0 GWh for 2011, made up of 240,209 kWh in the Residential class, 233,128 kWh in the GS<60kW class and 526,663 kWh in the GS>50kW class.[9]

Board staff submits that Parry Sound Power should use the 4 year target of 4.16 GWh and should not expect that in the test year, one quarter of this target will be realized. Rather, Board staff views 2011 as the CDM start-up year for Parry Sound Power. Board staff submits that 10% of the total 4 year target (4.16 GWh) should be used in the first year (2011). This was the conclusion reached by the Board in its recent Hydro One Brampton decision, EB-2010-0132. Accordingly, Board staff submits that Parry Sound Power should recast its load forecast by using this amount for the CDM impact.

Load Forecasting - Customer Growth

In terms of customer numbers, Parry Sound Power forecasts a slight increase of 1% in the test year, following similar 1% increases in 2010 and 2009. The proposed and actual customer numbers are set out in the table below.[10]

In terms of average use per customer, in the residential class, average use per customer has fallen since 2008: 11,886 kWh per customer in 2011 from 12,870 kWh in 2008, a drop of 7.6%. In the General Service <50 kW class, average use per customer has remained relatively constant since 2006. In the General Service >50 kW class, average use per customer has dropped by 4.7% from 2006 to the 2011 test year.

[9] Exhibit 3/Tab 2/Schedule 1/Table 3-6
[10] Exhibit 3/Tab 2/Schedule 1

As indicated in the table above, Parry Sound Power is forecasting a slight increase in Residential customer numbers, a slight decrease in GS<50kW customer numbers and a slight increase in GS>50kW customers for 2010 and 2011 as compared to 2009. Street lighting and Sentinel Light connections remain constant as do USL connections.

Based on the actual customer connections for 2010, as reported in response to VECC IR #34, it is apparent that the pre-filed evidence over-forecasted Residential customers by a small amount (21 customers). Differences in the other classes are minor.

Parry Sound Power
Customers, Actual and Forecast, 2006 - 2011

PARRY SOUND POWER Customers	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
Residential	2,610	2,643	2,697	2,744	2,778	2,812
GS< 50 kW	505	529	508	495	494	493
GS >50 kW	61	64	66	66	67	68
Streetlights* (connections)	1,004	1,004	1,004	1,004	1,004	1,004
Sentinel Lights (connections)	13	15	13	12	12	12
USL	20	22	17	18	18	18
Total (Res + GS only)	**3,176**	**3,236**	**3,271**	**3,305**	**3,339**	**3,373**
% change	0.3%	1.9%	1.1%	1.0%	1.0%	1.0%

Note: * Streetlight numbers updated as per Response to VECC IR # 34. Year end 2010 numbers were also provided in this IR response: 2,757 in Residential, 496 in GS<50kW and 66 in GS>50kW.

The Parry Sound Power pre-filed evidence indicated that the forecast of customer numbers for the Residential and GS<50kW customer classes was based on the geometric mean of customers for the periods 2004 through 2009. Parry Sound Power maintained that the geometric mean approach provides the average growth rate on a compounding basis.

The Applicant used the average change for 2008 - 2009 to predict the number of customers in the GS>50kW class for 2010 and 2011. As there are a relatively small number of customers in this class, a small change in the average number of customers can result in a large change in the number of forecast customers. Parry Sound Power forecasted no change from the 2009 number of customers for 2010 and 2011 for the Street Lights, Sentinel Lights, and Unmetered Scattered Load customer classes.

Board staff submits that although the actual customer numbers in 2010 differ slightly from forecast for 2010, the customer number forecast for the test year is reasonable.

OTHER DISTRIBUTION REVENUE

Parry Sound Power generates certain other distribution revenue which offsets its Service Revenue Requirement. Other distribution revenue is comprised of Specific Service Charges, Late Payment Charges, Other Distribution Revenues (Retail Services, Rent and Service Transaction Requests) and Interest and Dividend Income. Historical and proposed Other Distribution Revenues, which are an offset to the Service Revenue Requirement, are set out in the table below.

Parry Sound Power
Other Revenues, Actual and Forecast, 2006 - 2011

Parry Sound Power Other Distribution Revenue	2006 Board approved	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
Specific Service Charges	$48,569	$15,325	$27,504	$28,810	$26,150	$27,880	$27,880
Late Payment Charges	$17,448	$14,360	$16,906	$11,411	$17,984	$15,433	$15,433
Other Distributing Revenues	$18,376	$49,768	$53,252	$39,747	$52,276	$52,168	$52,168
Other Income and Expenses	$21,392	$123,362	$180,758	$151,417	$33,139	$5,505	$5,505
TOTAL	$105,785	$202,815	$278,420	$231,385	$129,549	$100,986	$100,986
% change		91.7%	37.3%	-16.9%	-44.0%	-22.0%	0.0%

Parry Sound Power shows a decrease in these additional revenues over the past few years. In 2010 and 2011 the relatively low level of other revenues is due to Parry Sound Power no longer including any non-utility revenues or forecast regulatory interest revenue (a $10,000 decrease) in the other revenue forecast.[11]

In addition, response to VECC IR #4c) indicates that interest income has fallen from 2008 as $2,068,724 in equity was transferred to the shareholder at that time. Parry Sound Power confirmed that it is not proposing any additional service changes for the test year.

Board staff has no submissions on the other revenues forecast.

[11] Exhibit 3/Tab3/Sch2/page 2

RATE BASE

Parry Sound Power is requesting approval of $5,967,046 for its 2011 rate base. For the 2007 to 2009 period, the Parry Sound Power rate base has declined each year until the Bridge Year. The historical and forecast rate bases are summarized in the table below.

Parry Sound Power
Rate Base, Actual and Forecast, 2006 - 2011

Parry Sound Power Rate Base	2006 Board approved	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
Gross Fixed Assets	$9,745,106	$10,478,190	$10,593,476	$10,905,755	$10,905,930	$11,083,150	$12,294,932
Accumulated Depreciation	$5,176,801	$6,106,367	$6,487,600	$6,761,274	$6,855,301	$6,966,329	$7,419,600
Net Book Value	$4,568,305	$4,371,823	$4,105,876	$3,944,481	$4,050,629	$4,116,821	$4,875,332
Average Net Book Value	$4,568,305	$4,503,933	$4,238,849	$4,025,179	$3,997,555	$4,083,725	$4,496,076
Working Capital	$6,494,285	$7,727,173	$7,716,086	$7,843,223	$7,991,868	$9,286,509	$9,806,469
Working Capital Allowance (WCA)	$ 974,143	$1,159,076	$1,157,413	$1,176,483	$1,198,780	$1,392,976	$1,470,970
Rate Base	$5,542,448	$5,663,009	$5,396,262	$5,201,662	$5,196,335	$5,476,701	$5,967,046
rate base year-on year inc.	na	2.2%	-4.7%	-3.6%	-0.1%	5.4%	9.0%
rate base (excl. WCA) year on year inc.		-1.4%	-5.9%	-5.0%	-0.7%	2.2%	10.1%

The significant increase in 2010 and 2011 over historical amounts is largely due to the increase in capital spending for transportation equipment in 2010 and higher capital spending in 2011 for Poles and Towers as well as a related expansion of conductor spending. In addition, the move to restructure the utility to meet ARC requirements has resulted in higher capital spending in the test year for Leasehold Improvements, Office Equipment and additional Transportation assets.

Parry Sound Power reported that it had used the full year rule for depreciation until the end of 2007 and then switched to the half year rule. In response to VECC IR #24, Parry Sound Power calculated the impact of this change as $38,700 for the test year. Ordinarily, Board staff would advocate that depreciation methodologies for regulatory purposes, remain constant through an IRM period, with the half year rule applied to the 2011 test year rate base, however, as the materiality threshold for a distributor with a revenue requirement of less than $10 million is $50,000, staff has no comment on this change in depreciation for the purposes of this application.

Regarding the Working Capital Allowance (WCA), Board staff takes no issue with Parry Sound Power's methodology (15% of specified amounts) for calculating the WCA for the test year. In response to VECC IR #19, Parry Sound Power provided an update of its cost of power, using the October 2010 RPP report.

Board staff submits that Parry Sound Power should update the WCA to reflect any changes in controllable expenses and load forecasts as determined by the Board in its Decision; the most current estimate of the RPP commodity price (ie, April 19, 2011) and updates to reflect current retail transmission prices. The material should provide sufficient detail and discussion to aid other parties in understanding the numbers provided and their derivation.

CAPITAL EXPENDITURES

The following table summarizes Parry Sound Power's historical and proposed capital expenditures as presented in the pre-filed evidence. In support of its proposed expenditures, Parry Sound Power filed a detailed Asset Management Plan, prepared by Rodan Energy Solutions.[12]

Board staff is of the view that the capital expenditures incurred between 2006 and 2009 have been adequately explained by the Applicant.

In response to Board staff supplementary IR #11, Parry Sound Power provided a year-end update to the 2010 capital expenditures, with a total of $581,613. This is $43,351 or 8 percent higher than in the original pre-filed evidence.

Significant increases were reported in the categories of Overhead Conductors (+30%), Underground conductors (+200%), Line transformers (+149%), Services (+287%) and Meters (+187%). A delay in the purchase of a pick-up truck resulted in a $27,498 reduction in the transportation equipment category.

[12] Exhibit 2/Tab 3/Schedule 2/ Appendix A

Parry Sound Power
Capital Expenditures, Actual and Forecast, 2006 - 2011

Parry Sound Power Capital Expenditures	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
	$	$	$	$	$	$
Distribution Station Equipment	14,909	-	419,407	3,930	12,785	-
Poles, Towers & Fixtures	24,567	27,609	47,057	124,286	139,039	414,729
O/H Conductors & Devices	22,956	12,965	94,747	56,979	36,663	236,195
Underground Conduit	24,151	238			5,058	64,178
U/G Conductors & Devices	28,143	9,514	11,566	1,287	9,351	-
Line Transformers	44,230	60,601	8,497	51,683	17,979	15,681
Services	14,759	25,856	26,121	20,185	4,021	-
Meters	13,709	10,781	42,787	152,960	9,119	-
Leasehold Improvements						200,000
Office Furniture & Equipment					10,062	38,499
Computer Equipment - Hardware				16,674	6,164	10,500
Computer Equipment- Software	-			63,433	26,873	7,000
Transportation	-				292,235	225,000
Tools, Shop & Garage					1,955	
Measure & Test Equipment						
Communication Equipment						
Miscellaneous Equipment						
Capital Contributions					-33,040	
TOTAL	$187,424	$147,564	$650,182	$491,417	$538,264	$1,211,782

Note: Does not include the amendments noted in the Argument-in-Chief, where $29,000 is added for 2010 and 2011, in Account 1855 - Services.

Board staff notes that if the 2010 actual capital spending of $581,613 is applied, the test year planned amount of $1,211,782 represents an increase of 108%.

In justifying this increase, response to Board staff IR #33 indicated that the primary reason was the requirement for conductor upgrades to increase system reliability and allow load transfers between substations without raising concerns regarding the overloading of the feeders/conductors.

Response to Board staff IR #35 dealt with the major capital expense ($641,778) in the test year, which is the first phase of the three year replacement of the MS1/MS2 municipal transformer station. The total three year cost is $2,340,220.

The rationale for replacing these two stations is that they have reached the end of their useful life and call for replacement. This need is clearly identified in the Asset Management Plan. The MS1/MS2 station was constructed in the 1960s and transformer nameplates identify the year of manufacture as 1968. The station is requiring increasing degrees of maintenance. The station provides service to the downtown business core as well as a large percentage of the residential customer base through ten (10) feeders (MS1 – 1-5) (MS2 – 6-10). In the event of a failure, there is not enough capacity between adjacent municipal stations to accommodate the load provided by the MS1/MS2 station.

The new station is planned to be constructed on an adjacent property and the existing MS1/MS2 station will remain in operation until the load can be transferred to the new station.

Information on the other major capital projects was provided through Board staff IR #36 Voltage Conversions ($47,000); and, #37 Conductor Replacements ($31,000).

The above mentioned projects are all designed to increase reliability in the Parry Sound Power distribution system. However, the reliability statistics do not show a consistent picture of decline, as shown in response to Board Staff IR #41, where SAIDI, SAIFI and CAIDI statistics from 2008 to 2010 are provided. Parry Sound Power also stated that no major outages occurred in 2010.

One other major capital expense category is the plan to spend $200,000 for office improvements in the building that Parry Sound Power has been using as a tenant but will be the leaseholder starting in 2011. Response to Board staff IR #36 indicates that, "*The $200,000 estimate is a minimum to update the 2400 sq. ft office, garage 1,040 sq. ft and 2,280 sq. ft of storage area. It is PSP's view that the existing building is aging and in need of major repairs."*

Another related expense is the purchase of Office Equipment and Computers which is budgeted at $39,999 and $7,000 in software in 2011. These office-related expenditures are also related to the effort to become a stand-alone utility in 2011.

Parry Sound Power also has plans to purchase a New Digger Derrick Truck for $225,000 to replace the existing 1990 truck.[13] Presumably, Parry Sound Power will

[13] Board Staff IR # 40

now also add the Pick-Up truck not purchased in 2010 to the 2011 plan. Board staff encourages Parry Sound Power to clarify this in its Reply Argument.

After considering all of the evidence presented the pre-filed evidence and interrogatory responses it appears to Board staff that the increase in Capital expenditures in the test year is too high as proposed. It also appears that Parry Sound Power may have difficulty ramping up capital expenditures to the degree requested for the test year. The proposed increase puts too much pressure on ratepayers, especially when considering the overall bill impacts resulting from this application.

Board staff suggest that if Parry Sound Power wishes to go ahead with the MS1/MS2 replacement project that it prioritize spending in other areas, such as other Pole and Fixture projects, Voltage Conversions and Conductor Replacements, doing only work on an ‘as needed’ basis until the 3 year MS1/MS2 project is complete. This planned work, in Board staff’s submission, could be cut back modestly from a total of $88,000 to $50,000, a saving of $28,000 in capital in the test year.

Board staff submits that as reliability statistics do not show a marked decline in performance, that restraint in capital spending in these areas will not have a marked affect in the short term.

In addition, Board staff submits that the purchase of the Derrick truck be delayed in the short term, so as to remove $225,000 in capital from the test year.

With regard to the investments proposed in building improvements, Board staff submits that the $200,000 capital cost is too high. Despite Parry Sound Power’s belief that the $200,000 cost of the improvements is a minimum amount, Board staff submits that a budget of $100,000 is more appropriate at this time for these improvements. This reduction leaves in place the related $47,000 Office equipment/computers and software budget.

In total, Board staff urges the Board to reduce the total capital budget for Parry Sound Power by $353,000 to a level of $858,782, which still a 41% increase from the 2010 bridge year actual.

OPERATING, MAINTEANCE AND ADMINISTRATION COSTS

A summary of Parry Sound Power's historic and projected Operating, Maintenance and Administration (OM&A) costs are shown in the table below.

Parry Sound Power
OM&A Costs, Actual and Forecast, 2006 - 2011

Parry Sound Power	2006 Board Approved	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
						(Actual)	
Operations	$ 66,823	$ 51,120	$ 63,190	$ 57,279	$ 57,300	$ 40,894	$ 17,801
Maintenance	$ 168,838	$ 213,937	$ 266,047	$ 268,637	$ 283,648	$ 214,887	$ 423,074
Billing & Collection	$ 283,052	$ 375,543	$ 342,691	$ 373,628	$ 380,463	$ 331,170	$ 395,022
Community Relations	$ 13,011	$ 30,656	$ 89,801	$ 52,381	$ 21,616	$ 14,918	$ 13,423
Administrative & General	$ 474,477	$ 365,288	$ 347,580	$ 464,189	$ 502,752	$ 566,683	$ 821,914
Total (adjusted)	**$1,006,201**	**$1,036,544**	**$1,109,309**	**$1,216,114**	**$1,245,779**	**$1,168,552**	**$1,671,234**
% Increase		**3.0%**	**7.0%**	**9.6%**	**2.4%**	**-6.2%**	**43.0%**

Note: 2010 has been updated with 2010 Actual results (Board staff IR #11) and also reduced in Operations by $29,000 (Argument-in Chief). For 2011, Maintenance is reduced by $95,184 and Operations reduced by $29,000 (Argument-in Chief).

Parry Sound Power proposed a Test Year OM&A budget of $1,795,418 which represented a 26.0% increase over 2010 (which was 14.4% higher than in 2009). These figures were amended for 2010 Actuals (Board staff IR #11) and submissions in the Argument-in-Chief to change the percentages to a 6.2% reduction in 2010 and a 43% increase in 2011. The 2011 level represents a 10.7% annual increase over 2006 Board approved. In its pre-filed evidence, Parry Sound Power provided explanations for the yearly variances over the 2006 to 2009 period.

As shown in the pre-filed evidence, the major drivers of the increase in 2011 are Labour costs (66%) and Regulatory Costs (32%). For 2010 the major driver was Materials costs offset by a reduction in Third Party costs.[14]

Response to Board Staff IR #11 indicated that Parry Sound Power's 2010 actual OM&A costs were $242,000 lower than indicated in the pre-filed evidence. The under-spending was mainly in the Maintenance category and was due to lower than planned work levels, inaccurate categorization of one project, removal of contingency costs and concern with allocated materials costs ($80,000).
For 2011 (after adjustments) it is apparent that the most significant increases are

[14] Exhibit 4/Tab2/Schedule 3/p. 1

found in the Maintenance (+$208,187 or 97%) and Administration & General Categories (+$255,231 or 45%). Board staff enquired about a number of 2011 maintenance project categories which showed the largest increases. These included Underground Distribution Lines & Feeders; Poles Towers and Fixtures; Overhead Conductors & Devices; Line Transformers: Overhead Services-Distribution Lines and Feeders. In responses provided to Board staff IRs #12, #13 and #14, Parry Sound Power provided further evidence justifying these costs by referencing specific projects as identified in the Asset Management Plan (AMP).

As for Administration & General, Board staff also questioned a number of areas: In Board staff IR #17, staff enquired about the 34% increase in General Administrative Salaries and Expenses, and Parry Sound Power replied that senior management (president and vice president/financial officer) were no longer shared between affiliated companies. Instead of only receiving 70% of the related wage and overhead costs, this will now change to 100% to achieve compliance as all of the senior management team costs and overheads are allocated to the distributor. Also included is a 3% wage increase and a new staff member, allocated at 30% to this category.

Board staff IR #18 enquired about the Office Supplies and Expenses account, which showed an increase from 2010 to 2011 of 21% after a 112% increase in 2010. Parry Sound Power's response was that due to restructuring to meet compliance with the ARC, these office supplies expense accounts, previously shared with the LDC affiliates, are now fully allocated to the distribution utility.

Another impact of the move to form a stand-alone utility, is that the Rent account under Administration & General grows to $69,527 an increase of 37% in the test year. Response to Board staff IR #20 shows that the Parry Sound Power building will no longer be shared and full cost of this space will be paid by the utility. Response to Board Staff Supplemental IR #6, indicated that Parry Sound Power will not rent out any part of the building as, "*The office and garage layout, without considerable renovations, does not suit the sharing of space model*."

As shown in the table above, Billing and Collection Costs increase 10% in the test year after falling 5.6% in 2009. Further information on these costs were provided in response to VECC IR #29.

Regulatory Costs

The Parry Sound Power pre-filed evidence shows regulatory costs of $210,929, up considerably from the 2010 level of $54,606 and from the 2009 level of $19,427.[15] Responses to Board staff IR #21 and Supplemental IR #7 provided a clear picture of how these costs were calculated:

[15] Exhibit 4/Tab 2/Schedule 2/ page 3

2009 Cost of Service Application (withdrawn)		$ 99,315	
2011 Cost of Service Application		$176,258	
Asset Management Plan costs		$123,249	
ARC Compliance/Corporate Changes		$158,407	
Sub-Total		$557,230	
Divided by the 4 year IRM period:			$139,307
Other Regulatory Costs: ESA, OEB, Reg. Advertising			$ 19,347
Existing Labour/OH staff at 20%	$11,650		
New hire + overhead at 50%	$40,625		$ 52,275
Grand Total			$210,929

Information on the 2009 Cost of Service application that was withdrawn, was provided in the pre-filed evidence.[16] Parry Sound Power indicated that in 2008, it filed a self-nomination request for rebasing in 2009 and then filed a complete cost of service application on August 18, 2008 for rates effective May 1, 2009. (EB-2008-0240). Due to matters beyond Parry Sound Power management control this application was withdrawn.

The activities that were undertaken to achieve ARC Compliance and related costs were described in Board Staff IR #32, supplementary Board staff IR #10 and supplementary VECC IR # 42b.

Staffing and Compensation

In the pre-filed evidence, Parry Sound Power showed a staffing complement of 12.5 FTEs for the test year and a total compensation amount of $1,067,550. In response to Board Staff IR #25, Parry Sound Power provided historical staffing and compensation figures as shown in the table below.

[16] Exhibit 1/Tab 1/Schedule 7/ page 1

Parry Sound Power
Staffing & Compensation, Actual and Forecast, 2006 - 2011

Parry Sound Power	2006 Board approved	2009 Actual	2010 Bridge Year	2011 Test Year
Employees (FTE)				
Non-Union	3	3	3	4
Union	5	6	7	8.52
Total	7.6	8.57	9.94	12.52
yearly change		0.97	1.37	2.58
Total Compensation				
Non-Union	$ 323,367	$ 365,501	$ 250,773	$ 338,188
Union	$ 281,079	$ 320,148	$ 470,043	$ 729,362
Total	$ 604,446	$ 685,649	$ 720,816	$ 1,067,550
yearly change %				
Non-Union		13.0%	-31.4%	34.9%
Union		13.9%	46.8%	55.2%
Total		13.4%	5.1%	48.1%

In the response to Board Staff supplementary IR #8, Parry Sound Power explains the overall increase in compensation from 2010 to 2011 by citing a 3% inflationary increase, ($21,625) one new hire ($81,250) and a switch of allocated staff to the wires only company ($243,859).

As noted above, response to Board staff IR #17 indicated that senior management (president and vice president/financial officer) were no longer shared between affiliated companies. Instead of only receiving 70% of the related wage and overhead costs, 100% of the senior management team costs and overheads are now allocated to Parry Sound Power. In addition, a 3% wage increase and a new 30% allocated staff member is included. Response to Board staff Supplementary IR #4 also indicated that the additional staff member would be allocated 50% to regulatory and 20% to Billing & Collections.

Response to Board staff Supplementary IR #9 indicates that Parry Sound Power omitted an increase of $7,934 for OMERS expenses in the test year. It is not clear whether Parry Sound Power has included this additional cost in its Argument-in-Chief and Board staff invites Parry Sound Power to address this issue in its Reply Argument.

OM&A per Customer
In response to Board staff supplementary IR #2, Parry Sound Power provided a table that compares OM&A per customer statistics with its Small Northern Low Undergrounding Cohort of 9 LDCs. The evidence shows a consistent pattern of Parry Sound Power in the middle of this cohort, most recently 5th highest in 2008 and 2009. When the impacts of this application are included, Parry Sound Power's OM&A per customer will grow from $369 in 2009 to $493 in 2011 (as amended in Argument-in-Chief), an increase of 34%.

Customers per FTE
In response to VECC supplementary IR #42b, Parry Sound Power provided data on Customers per FTE for 16 utilities in Ontario, of which 6 were in the Parry Sound Power Cohort. With this admittedly incomplete sample, Parry Sound Power (at 270 customers per FTE) was 4th out of the six distributors in its cohort and 14th of 16 in the entire group of 16. In Board staff's view this shows that there is some need for improvement on the part of the Applicant.

Parry Sound Power Argument-in-Chief
On April 13, 2011 Parry Sound Power filed its Argument-in-Chief, providing a final clarification of the application in response to factors revealed in the interrogatory process.

Parry Sound Power proposed to remove the 'congruency' amount and the material components of certain projects identified in the Asset Management Plan. These adjustments, to projects 5f, 6c, 6i, 6j and 6k, result in a reduction in the OM&A Maintenance costs in the test year of $95,184.40. Also, Parry Sound Power now proposes to move $29,000 from Operations to Capital in account 1855 for both the Bridge and Test Years. Board staff is unclear as to the rationale for this move and invites Parry Sound Power to clearly address the reasons for this change in its Reply Argument.

These changes would reduce the Maintenance budget for 2011 from $518,258 to $423,074. The Operations budget for 2011 would fall from $45,801 to $17,801 and for 2010 would fall from $54,737 to $25,737. Services capital would increase by $29,000 in each year bringing the 2010 Capital amount to $567,263 and to $1,240,782 in 2011.
Overall, Parry Sound Power submitted that its revenue requirement for the test year would fall from $2,714,942 to $2,592,355.

<u>Board Staff Submissions on OM&A</u>
Board staff is encouraged that Parry Sound Power has amended its OM&A budget for the test year, as it appeared that the original applied-for increase at 54% over the bridge year actual was unjustifiable. Even with the amendments as filed by

Parry Sound Power, the OM&A increase is still extremely high at 43%. Moreover, a bill impact of 9.7% is still quite large. Despite these reductions, Board staff is of the view that some of the increases in the Parry Sound Power OM&A budgets are still not justifiable. Board staff submits that reductions are justifiable in the following areas:

Regulatory Costs

Parry Sound Power has submitted for a recovery of costs of $99,315 for the rates application withdrawn in 2009[17]. Board staff submits that it is inappropriate for these costs to be recovered in a 2001 application. These are prior period costs for which no deferral or variance account treatment was granted and therefore should not be granted in this proceeding.

Another category within regulatory costs for which Board staff has a concern is the cost noted for ARC Compliance and Corporate restructuring. The total cost claimed is over $158,000 or over $47 per customer. In reviewing the response to VECC IR #42b, it appears to Board staff that a number of the activities undertaking for the reorganization are activities that are usually undertaken in the normal business of a distribution utility, such as development of a 4 year strategic plan, the asset management plan already submitted separately for recovery, determining spacing requirements for administration and operations, and time analyses for customer support personnel.

Board staff also notes that the decision on Parry Sound Power's ARC exemption application (EB-2009-0133) was issued on November 15, 2009, while the Board issued its revised Affiliate Relationships Code on March 15, 2010. Board staff invites Parry Sound Power to comment on how the revised ARC influenced its decisions on ARC Compliance and Corporate Restructuring, in its Reply Argument.

Board staff submits that costs for some of these activities are too high and should not be the responsibility of ratepayers in a special 4 year recovery of regulatory costs. Board staff submits that 25% of these claimed costs or $40,000 be removed from the costs of ARC compliance.

Board staff also submits that for a distributor the small size of Parry Sound Power, the addition of a half-time regulatory staff person, on top of the current .20 FTE position is excessive. While it can be argued that some additional resources are required, this more that doubling of the Regulatory compliment is not justified. Accordingly, Board staff submits that only a .30 FTE increase be allowed for recovery by ratepayers.

Board staff calculates that these three reductions will result in lowering the Regulatory Affairs budget by $62,722; ($34,828 annual impact of the 2009

[17] Board Decision, EB-2008-0240, November 28, 2008, p. 2

recovery and the reduction in ARC compliance costs and a $27,894 reduction due to .30 FTE change).

Staffing and Compensation

The table above shows that staff numbers grow from 9.94 in 2010 to 12.52 in 2011, an increase of 2.58 FTE positions in one year, or 26%. At the same time compensation costs grow by 48%, or $346,734. With simple division this yields a per position increase of $137,592. With inflation in the application assumed at 2.2 %[18] , these compensation increases appear completely inappropriate.

Staff had already recommended a reduction of a .20 FTE position for regulatory and now also submits that an additional FTE should be removed, leaving an increase of 1.32 FTE for the test year, a reasonable increase by any measure for a smaller distributor. Board staff submits that at least $100,000 be removed from the OM&A compensation budget and is of the view that this can be reasonably managed in the following ways:

- the movement of Senior Management staff from 70% to 100% allocation provides additional resources,

- the 3% compensation increases assumed in the application are above current industry wage increases. Board staff notes that under the Board's current IRM proceedings utilities are expected to manage costs within the 1.3% price escalator.

Administration and General Costs

As shown in the OM&A table above, Administration and General Costs increase by 45% in the test year, from 2010 actual costs. This is an amount over $255,000. As noted above, questions were raised about significant increases in Office Supplies and Expenses, Rent costs and Billing & Collection costs. In all instances the impact of the efforts to become a stand alone distribution utility is cited as a rationale for these increased costs. Board staff submits that Parry Sound Power has not demonstrated enough effort to control the costs of restructuring and submits that the Office Supplies & Expenses and Rent costs should be reduced by $10,000 in the test year.

In summary, the total OM&A reduction of $163,133 recommended by Board staff will work to reduce the OM&A 2010/2011 increase from 43% to 29%. While still a very high increase, considering that the operation of a stand alone utility does incur additional costs, Board staff sees this as a reasonable OM&A level.

Board staff notes that the recommended OM&A level falls to $444 per customer as

[18] Response to Board staff IR #9

compared to the applied for $493 per customer, only 20% higher than the 2009 score and 9% above the cohort average for 2009.

At noted above, Board staff is not clear on how the OMERs cost increase is to be treated by Parry Sound. Board staff encourages Parry Sound Power to clarify these amounts in the requested revenue requirement, in its Reply Argument.

Amortization and Depreciation

Board staff does not have any concerns with the amortization/depreciation amounts proposed by Parry Sound Power. In the event the Board makes changes to Parry Sound Power's capital expenditures, Board staff submits that the Board in its decision should direct Parry Sound Power to reflect the impact on amortization/depreciation in its draft Rate Order.

Provision for Payments in Lieu of Taxes

Parry Sound Power filed its Payments in Lieu of Taxes (PILs) evidence at Exhibit 4/Tab3/Schedule1. The calculated PILs provision for the test year is $47,696. Response to Board staff IR #47 included a number of items providing background information pertaining to the PILs provision and tax filings for 2009, 2010 and 2011. Board staff has no concerns with the income tax calculations provided by the Applicant.

COST OF CAPITAL

Parry Sound Power is proposing a test year weighted cost of capital of 8.08% based on a deemed capital structure which is consistent with the Board's guidelines.[19] See the summary table presented below.

Parry Sound Power
2011 Test Year Cost of Capital

	Amount (Rate Base)	Weight	Cost Rate	Weighted Cost	Return
Long Term Debt	$ 3,341,546	56%	7.25%	4.06%	$ 242,262
Short Term Debt	$ 238,682	4%	2.07%	0.08%	$ 4,941
Total Debt	$ 3,580,228	60%			$ 247,203
Common Equity	$ 2,386,819	40%	9.85%	3.94%	$ 235,102
TOTAL	$ 5,967,047	100%		8.08%	$ 482,304

[19] Exhibit 5/Tab1/Schedule 1 p. 3

Board staff notes that Parry Sound Power has acknowledged that the cost for Short term Debt and ROE reflected in the table above will likely be amended when the Board releases its revised rates, which it did on March 3, 2011. Board staff notes the applicable Short term Debt Rate is 2.46% and the Common Equity rate is 9.58%.

Parry Sound Power is proposing a long term debt rate debt rate of 7.25% and has indicated that it currently has a Long Term Loan with its Shareholder, the Town of Parry Sound, with a value of $2,433,728. Board staff notes that the remaining long term debt amount of $907,818 is not addressed in the evidence and the debt instruments and applicable interest rates for this amount is also not apparent. Board staff submits that Parry Sound Power should identify the other debt instruments that make up this difference in its Reply Argument. If there are no identifiable debt instruments, then this residual long term debt should be assigned the Board's current long term debt rate of 5.32%.

With regard to the Long Term Debt held by the Town of Parry Sound, Board staff refers to the Board's December 11, 2009 Cost of Capital report (EB-2009-0084) which provides guidance on the characteristics of the Long Term debt. On pages 53 and 54 of that report:

> **"The Board will primarily rely on the embedded or actual cost for existing long-term debt instruments**. The Board is of the view that electricity distribution utilities should be motivated to make rational decisions for commercial "arms-length" debt arrangements, even with shareholders or affiliates.
>
> In general, the Board is of the view that the onus is on the electricity distribution utility to forecast the amount and cost of new or renewed long-term debt. The electricity distribution utility also bears the burden of establishing the need for and prudence of the amount and cost of long-term debt, both embedded and new.
>
> Third-party debt with a fixed rate will normally be afforded the actual or forecasted rate, which is presumed to be a "market rate". However, the Board recognizes a deemed long-term debt rate continues to be required and this rate will be determined and published by the Board. **The deemed long-term debt rate will act as a proxy or ceiling for what would be considered to be a market-based rate by the Board in certain circumstances**. These circumstances include:
>
> - For affiliate debt (i.e., debt held by an affiliated party as defined by the Ontario *Business Corporations Act, 1990*) with a fixed rate, the deemed

long-term debt rate at the time of issuance will be used as a ceiling on the rate allowed for that debt.

- For debt that has a variable rate, the deemed long-term debt rate will be a ceiling on the rate allowed for that debt. This applies whether the debt holder is an affiliate or a third-party.

- The deemed long-term debt rate will be used where an electricity distribution utility has no actual debt.

- For debt that is callable on demand (within the test year period), the deemed long-term debt rate will be a ceiling on the rate allowed for that debt. Debt that is callable, but not within the period to the end of the test year, will have its debt cost considered as if it is not callable; that is the debt cost will be treated in accordance with other guidelines pertaining to actual, affiliated or variable-rate debt.

- A Board panel will determine the debt treatment, including the rate allowed based on the record before it and considering the Board's policy (these Guidelines) and practice. The onus will be on the utility to establish the need for and prudence of its actual and forecasted debt, including the cost of such debt."

And, on page 59 of that report,

> "For new affiliated debt, the deemed long-term debt rate will be a ceiling on the allowed rate. The onus will be on the utility to demonstrate that the applied for rate and terms are prudent and comparable to a market-based agreement and rate on arms-length commercial terms."

It is Board staff's submission that Parry Sound Power has not established that the cost of this affiliated debt is prudent or comparable to a market based agreement and rate on arms-length commercial terms.

Board staff submits that the appropriate interest rate that should apply to Parry Sound Power's affiliate debt is the Board's current deemed long term debt rate of 5.32% for rates effective May 1, 2011, as documented in the Board's letter of March 3, 2011. Board staff submits that Parry Sound Power should provide reasons for why this affiliated debt amount of $2,433,728 should not attract the Board's long term deemed debt rate of 5.32% in its Reply Argument.

Board staff notes that applying the Board's deemed long term debt rate to Parry Sound Power's long term debt amount, will work to reduce the revenue requirement by approximately $65,000.

COST ALLOCATION AND RATE DESIGN

In its pre-filed evidence Parry Sound Power indicated that it had used the Board-approved Cost Allocation Model and followed the instructions and guidelines issued by the Board to enter the 2011 data into this model. It also made the changes to the Transformer Allowance and Low Voltage treatments according to the latest filing guidelines issued by the Board for the 2011 Cost of Service rate applications.[20]

Revenue to Cost Ratios

Parry Sound Power's proposed Revenue to Cost ratios are set out in the table below:

Parry Sound Power
Revenue to Cost Ratios, 2011

Parry Sound Power Rate Class	Updated OEB Cost Allocation Model, R/C Ratios	Proposed Revenue to Cost Ratios		Board Target Low	Board Target High
Residential	102%	102%		85%	115%
GS <50kW	85%	85%		80%	120%
GS>50kW	148%	141%		80%	180%
Sentinel Lighting	40%	70%		70%	120%
Streetlighting	14%	28%		70%	120%
USL	46%	80%		80%	120%

Parry Sound Power proposed to re-align its revenue to cost ratios by adjusting the revenue allocations among rate classes in order to reduce cross-subsidization. The proposed re-alignment will move the Sentinel Lighting and Unmetered Scattered Load classes to the lower end of the Board target ranges.

To mitigate the impact on the Street Lighting class, Parry Sound Power followed the Board direction provided to other LDCs in previous Cost of Service decisions and therefore has moved the Street Light class to a Revenue to Cost Ratio of 28% for 2011 with the intention of moving to the 70% target over the term of the future IRM period.

Parry Sound Power also proposed that the Street Lighting class move to revenue to cost ratios of 42%, 56%, and to 70% in the years 2012, 2013, and 2014 respectively. These upward revenue to cost ratio adjustments result in the need to decrease the R/C ratios in other classes. Therefore, the General Service >50kW

[20] Exhibit 7/Tab1/Schedule 2, p. 3

class is adjusted from 148% to 141%, since the only other remaining customer class that exceeds a revenue to cost ratio of 100% is Residential which is relatively close to unity at 102%.

Board staff submits that the progress to move the Streetlight class into the Board range should be accelerated and should be completed in two years and not four years.

Monthly Fixed Charges and Variable Distribution Rates
Parry Sound Power's current and proposed fixed monthly and variable distribution rates are presented in the table below[21].

Parry Sound Power
Fixed and Variable Charges, 2010 and 2011

Parry Sound Power Rate Changes	Monthly Service Charge Current	Monthly Service Charge Proposed		Variable Charge Current	Variable Charge Proposed
Residential	$16.79	$23.97	kWh	$0.0134	$0.0191
GS <50kW	$25.29	$36.01	kWh	$0.0104	$0.0148
GS>50kW	$171.14	$237.51	kW	$3.4592	$4.6012
Sentinel Lighting	$1.74	$4.92	kW	$6.7501	$19.0674
Streetlighting	$0.41	$1.27	kW	$4.1163	$12.7683
USL	$8.96	$23.33	kWh	$0.0523	$0.1362

Parry Sound Power proposed to maintain the current fixed/variable split for its 2011 rates. These fixed/variable splits are:

Class	Volumetric	Fixed
Residential	44.15%	55.85%
GS<50kW	53.76%	46.24%
GS>50kW	69.92%	30.08%
Sentinel Lights	49.26%	50.74%
Streetlights	65.62%	34.38%
USL	61.35%	38.65%

In response to VECC IR #8 Parry Sound Power addressed the fact that the monthly service charge for the General Service >50kW class exceeds the ceiling

[21] Exhibit 8/Tab1/Schedule 2

value established by the Board in its EB-2007-0667 Report.

Parry Sound Power indicated that its proposed fixed monthly rates are consistent with the Board's guidance found in the *Board Report on the Application of Cost Allocation for Electricity Distributors* (EB-2007-0667), November 28, 2007. The proposed monthly fixed rates are above the ceiling amount for this class as it is Parry Sound Power's understanding of the current regulatory status is that distributors are not required, for the time being, to make changes to their monthly fixed rate when they exceed the ceiling.

Parry Sound Power provided a history of the Board's activity concerning the question of fixed/variable split and referred to the Board's Norfolk Power Distribution Inc. Decision EB-2007-0753. Parry Sound Power submitted that an MSC ceiling has not been established and that it is appropriate to keep the current variable/fixed split.

In the response to VECC supplementary IR #35, Parry Sound Power further defended the decision to increase this monthly fixed charge above the stated ceiling and presented a table of MSC charges in its cohort of distributors for the GW>50kW class to show that the proposed rate was in the middle of the rates established in this cohort.

Board staff does not have any concerns with Parry Sound Power's fixed monthly rates as proposed.

Loss Factors

Parry Sound Power provided evidence[22] showing that its average (2004-2009) distribution loss factor was 1.0453. The supply facility loss factor is 1.0340. These loss factors equate to a 1.0809 Total Loss Factor for a Secondary Metered Customer <5,000 kW and a 1.0700 for a Primary Metered Customer <5,000 kW. Parry Sound Power accordingly requested a loss factor change from the existing levels of 1.0586 and 1.0480 respectively. Board staff notes the significant change in loss factor and submits that Parry Sound Power investigate the reasons for this change and address this in its Reply Argument. If this change cannot be explained then Board staff submits that the Board should order Parry Sound Power to complete a loss factor study to address this issue.

RETAIL TRANSMISSION SERVICE RATES

Parry Sound Power is proposing to revise its Network Service and Line and Transformation Connection rates, using the RTSR Workform pursuant to the Board's guidelines for electricity distribution Retail Transmission Service rates (G-2008-0001) Revision 2.0.[23]

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[22] Exhibit 8/Tab1/Schedule 5
[23] Exhibit 8/Tab1/Schedule 3

Parry Sound Power noted that these rates would be subject to modifications, should the UTR rates change early in 2011. Board staff notes that on January 18, 2011 the Board issued its Rate Order for Hydro One Transmission (EB-2010-0002) which adjusted the UTRs effective January 1, 2011. The new UTRs are shown in the following table:

Uniform Transmission Rates	kW Monthly Rates		Change
	Jan 1, 2010	Jan 1, 2011	
Network Service Rate	$2.97	$3.22	+8.4%
Connection Service Rates			
Line Connection Service Rate	$0.73	$0.79	
Transformation Connection Service Rate	$1.71	$1.77	
			+4.9%

Board staff submits that Parry Sound Power update its proposed RTSR rates reflecting these new rates and that Parry Sound Power include this information, along with the completed RTSR module, in its reply submission.

LOW VOLTAGE CHARGES

Parry Sound Power is an embedded distributor with Hydro One Networks Inc. and is subject to Low Voltage (LV) charges. In its pre-filed evidence, Parry Sound Power indicated that the 2008 audited balance of variance account 1550 was disposed of as part of the 2010 IRM rate application.

The 2009 accumulated principal balance is a credit of $1,312 which is being disposed of in this rate application. It is Parry Sound Power's position that since the accumulated amount is relatively small, it proposes to continue with the current approved LV rates. Parry Sound Power forecast the Low Voltage revenues at the proposed rates for the test year to be $82,266. This amount was used in the calculation of the Cost of Power.

Board staff has no issues with Parry Sound Power's LV rates proposal.

SMART METERS

In its pre-filed evidence[24], Parry Sound Power requested a smart meter funding adder of $1.71 per metered customer per month to replace its current standard smart meter funding adder of $1.00. Very little smart meter detail was originally filed, but additional information was provided in the interrogatory process. Subsequently, Parry Sound Power revised its smart meter funding adder proposal

[24] Exhibit 9/Tab 1/Schedule 3

to $2.88 per metered customer per month, in response to supplementary VECC IR #37.

In that same response, Parry Sound Power showed that its residential and small commercial (GS<50 kW) installations in total were substantially complete (2,779 residential and 512 small commercial) and reported an average installed cost of $288.86 per meter. Board staff notes that this per meter cost appears to be high compared to other distributors in Ontario, but within the range of reasonableness when considering distributors located in Northern Ontario.

Board staff notes that in the Board's 2011 IRM decisions where the applicant requested an increase to their smart meter funding adder in excess of $2.50 per metered customer per month, the Board indicated that:

> "The Board notes that the SMFA is a tool designed to provide advance funding and to mitigate the anticipated rate impact of smart meter costs when recovery of those costs is approved by the Board. The Board also observes that the SMFA was not intended to be compensatory (return on and of capital) on a cumulative basis over the term the SMFA was in effect. The SMFA was initially designed to fund future investment, not fully fund prior capital investment. In the Board's view, the funding of prior capital investment would increase the risk, absent a prudence review, of over recovery. The Board is not saying that prudently incurred costs are not recoverable; it is stating that a determination of full recovery will be made as part of an application for a prudence review.
>
> The Board is also concerned about the rate impact associated with the level of the proposed increase in the SMFA. Since the deployment of smart meters on a province-wide basis is now nearing completion, and for the reasons noted earlier, the Board expects distributors to file for a final prudence review at the earliest possible opportunity following the availability of audited costs. For those distributors that are scheduled to file a cost of service application for 2012 distribution rates, the Board expects that they will apply for the disposition of smart meter costs and subsequent inclusion in rate base. For those distributors that are scheduled to remain on IRM, the Board expects these distributors to file an application with the Board seeking final approval for smart meter related costs. In the interim, the Board will approve a SMFA of $2.50 per metered customer per month from May 1, 2011 to April 30, 2012. This new SMFA will be reflected in the Tariff of Rates and Charges, and will cease on April 30, 2012."

Board staff therefore submits that the Board might consider approving a smart meter funding adder of $2.50 per metered customer per month from May 1, 2011 to April 30, 2012.

<u>Stranded Meters</u>
Parry Sound Power is not seeking the recovery of the stranded meter costs but has stated that it is waiting for direction from the Board with respect to the method of

recovery.[2] In response to Board staff IR #46, Parry Sound Power reported that it has kept the record of stranded meter costs in Account 1860 and that it no longer amortizes these costs. The residual net book value of these meters at December 31, 2009 is $161,416.68. Parry Sound Power also reported that the depreciation expense that would be applicable for the period from the time the meter became stranded to December 31, 2009 is $12,071.41.

Board staff notes that Parry Sound Power will be receiving rate base treatment on most of its smart meters that have replaced its “stranded” meters. Consistent with the Board’s decision and order for Hydro One Brampton Networks Inc. (EB-2010-0132), Board staff submits that it is no longer appropriate for the distributor to receive a concurrent rate base treatment for stranded meters that are no longer used and useful. Board staff submits that at this time, a simpler and more appropriate approach from an accounting perspective for the recovery of stranded meters costs may be to allow recovery of the estimated residual net book value of the overall stranded meters. The estimated amount should comprise the pooled residual net book value of the removed from service meters, less any sale proceeds and contributed capital, as of April 30, 2011 or the day before the effective date of the 2011 rate order.

Pursuant to the Board’s EB-2010-0132 decision and order, Board staff further submits that the total estimated stranded costs as of April 30, 2011 could be allowed to be recovered through a separate rate rider. If this proposal is adopted by the Board, Parry Sound Power should revise this estimate to the end of 2011 to reflect information that is more current. Parry Sound Power may wish in its reply submission to suggest a reasonable recovery period. Board staff also submits that the estimated total costs related to the stranded meters in rate base on approval for recovery be removed from rate base (and Account 1860, Meters) and tracked in “Sub-account Stranded Meter Costs” of Account 1555. The associated recoveries from the separate rate rider should also be recorded in this sub-account to draw down the balance in the sub-account. The approved estimate of stranded meter costs should be trued-up to actual costs, recorded in the sub-account, and submitted for review in the distributor’s next cost of service application. A final disposition of the sub-account balance (comprised of the final stranded meter costs as of April 30, 2011 net of the rate rider recoveries) would be addressed in that proceeding.

Board staff invites parties to comment on the recovery methodology for the stranded meter costs, the proposed recovery period, and the associated bill impacts.

DEFERRAL AND VARIANCE ACCOUNTS

Parry Sound Power provided a list of the Deferral and Variance accounts currently in use and requested disposition of the account balances representing principal balances to December 31, 2009 and projected interest to April 30, 2011. This is summarized in the table below:

Account Number and Description	Total Claim[25]
1550 – Low Voltage Account	($1,642)
1580 – RSVA – Wholesale Market Service Charge	($26,582)
1584 – RSVA – Retail Transmission Network Charge	($16,546)
1586 – RSVA – Retail Transmission Connection Charge	($36,418)
1588 – RSVA – Power (excluding Global Adjustment)	$1,190,682
1588 – RSVA – Power – Sub-account Global Adjustment	($690,078)
1590 – Recovery of Regulatory Asset Balances	($69)
Group 1 Subtotal	**$419,347**
1508 – Other Regulatory Assets	$11,425
1518 – RCVA – Retail	($3,862)
1548 – RCVA – STR	$53
1582 – One-time Wholesale Market Service	$15,322
Group 2 Subtotal	**$22,938**
TOTAL	**$442,285**

The balances as of December 31, 2009 are consistent with Parry Sound Power's RRR filings with the Board. Board staff has no issues with the balances requested for disposition, but does note that there is a significant balance in Account 1582 – One–time Wholesale Market Service and invites Parry Sound Power to address the reasons for this balance in its Reply Argument.

Disposition Period

In its pre-filed evidence[26], Parry Sound Power requested a one-year rate rider to recover the deferral and variance account balances. In response to Board staff IR #2, Parry Sound Power filed a bill impact analysis, which showed the bill impact of over 16% on a residential bill with a monthly consumption of 800 kWh. Subsequently, Parry Sound Power provided the bill impacts based on a 2-year and a 4-year rate rider, as per Board staff supplementary IR #17. The total bill impact, based on a 2-year and 4-year rate riders will be approximately 12.5% and 10.6% respectively.

In its Argument-in-Chief, Parry Sound Power changed its proposal to recover the deferral and variance account balances over a 4-year period. Parry Sound Power made some additional revisions to its original application, reducing certain other costs, and revised the rate impact based on 4-year disposition to 9.67%.

[25] Exhibit 9/Tab 1/Schedule 2, page 1
[26] Exhibit 9/Tab 1/Schedule 2, page 1

Board staff submits that a 4-year disposition is appropriate in this case, as the bill impact with a shorter disposition period is above the 10% bill impact mitigation threshold historically used by the Board.

Global Adjustment

In its pre-filed evidence, Parry Sound Power did not calculate a separate rate rider for global adjustment. In response to VECC IR #12a), Parry Sound Power stated that although it did not calculate a specific rate rider; it did take into consideration the non-RPP kWh as a basis of the allocation of the Global Adjustment. This approach is consistent with EDDVAR, and spreads the recovery of the allocated account balances to all customers in the affected rate class.

Board staff submits that the Board may wish to consider establishing a separate rate rider for the disposition of the global adjustment sub-account balance enabling the prospective recovery solely from non-RPP customers, as this would be more reflective of cost causality as it was that group of customers that was responsible for accumulation of balances in this account. Board staff suggests that Parry Sound Power in Reply Argument, comment on its ability to recover these balances in this manner or advise when they expect to be able to do so.

Alternatively, Board staff suggests that the Board may wish to consider the recovery of the allocated global adjustment sub-account balance from all customers in each class, as this approach would recognize the customer migration that might occur both away from the non-RPP customer group and into the non-RPP customer group.

HARMONIZED SALES TAX

In response to Board staff IR #57, Parry Sound Power stated that it has accounted for reductions in both OM&A and capital expenditures related to the harmonization of PST and HST.

In response to VECC IR #31, Parry Sound Power stated that it has not separated PST from OM&A expenditures for 2007, 2008, 2009 or 2010.

In addition, Parry Sound Power indicated that it had not recorded any incremental input tax credits in account 1592 as this would be extremely labour intensive and that their current financial system cannot accommodate such segregation within an invoice. Parry Sound Power confirmed that the HST on invoices received is recorded as an input tax credit.

Board staff notes that the Board's EB-2009-0207 IRM Rates decision, dated April 28, 2010, directed Parry Sound Power to:

> "…beginning July 1, 2010, Parry Sound shall record in deferral account 1592 (PILs and Tax Variances, Sub-account HST / OVAT Input Tax Credits (ITCs)) the incremental ITC it receives on distribution revenue requirement items that were previously subject to PST and become subject to HST. Tracking of these amounts will continue in the deferral account until the effective date of Parry Sound's next cost of service rate order. 50% of the confirmed balances in the account shall be returnable to the ratepayers."

Board staff submits that Parry Sound Power should comply with the 2010 IRM decision of the Board, however, given the advanced stage of this proceeding, and the relative magnitude of the amount and which would need to be scrutinized, Board staff believes that examination and disposition of this amount should be considered in a subsequent proceeding.

Staff notes that the review and disposition of account 1592 is not typically within the scope of an IRM proceeding. Staff submits that the Board may wish to consider that due to the nature of the costs tracked in this sub-account that this sub-account be brought forward for disposition in the next rate proceeding for Parry Sound Power, which would be Parry Sound Power's 2012 IRM application.

Delaying disposition of this sub-account until Parry Sound Power's next rebasing application (2015) would represent an unreasonably long delay in providing customers with the benefit of the ITCs. Staff also notes that this is a generic issue that would apply to all applicants that have a deferral account for ITCs and that are scheduled to file an IRM application for 2012 rates.

LRAM/SSM

Parry Sound Power's proposal for a Lost Revenue Adjustment Mechanism and Shared Savings Mechanism is found in the pre-filed evidence at Exhibit 10/Tab 1/Schedule 1. In support of this proposal, Parry Sound Power submitted a report prepared by Burman Energy Consultants Group.

The amounts sought for recovery in 2011 rates for LRAM and SSM were $96,367.42 and $2,399.42 respectively. In response to VECC IR #17, Parry Sound Power provided a revised calculation of the LRAM recovery: $109,069.49. In response to VECC supplementary IR #39, Parry Sound indicated that it seeks to recover the revised amount. It appears that Parry Sound Power has used the most recent OPA assumptions and measures in the calculation of its revised recovery amount.

Board staff submits that Parry Sound Power confirm that it has amended its proposal for the LRAM/SSM in its Reply Argument.

Low Income Energy Assistance Program (LEAP)

In response to Board Staff IR #22, Parry Sound Power indicates that it has not included LEAP funding in its application. The calculation of 0.12% of total distribution revenue ($2,714,943) is also provided in this response ($3,257.93).

Board staff note that this calculation is consistent with the Board's guidance found in its letter on LEAP Emergency Financial Assistance dated October 20, 2010.

Board staff submits that Parry Sound Power should update this calculation in accordance with the approved revenue requirement resulting from the Board's decision on this application, and include it in the revenue requirement.

Late Payment Penalty (LPP) Litigation Costs

On February 22, 2011 the Board issued its generic decision and order, file EB-2010-0295, regarding the recovery from ratepayers of the costs and damages incurred in the Late Payment Penalty Class Action.

In response to Board Staff IR#23, Parry Sound Power indicates that it has not included these costs in its application. However, on March 3, 2011 Parry Sound Power provided its response to the Board's February 22, 2011 Decision indicating that the LPP amount for recovery from customers was $12,417 and also provided the calculations to establish Monthly Fixed Charge Rate Riders for each customer class. Parry Sound Power corrected the customer numbers on April 21, 2011 and consequently, Board staff has no issues with the calculation of these rate riders.

RATE AND BILL IMPACTS

In response to Board staff IR#2, Parry Sound Power corrected its initial pre-filed bill impact evidence and showed a total bill impact of over 16% on a residential bill with a monthly consumption of 800 kWh (39% on the delivery line). Subsequently, and as noted above, Parry Sound Power provided bill impact analyses based on a 2-year and a 4-year deferral and variance account disposition. The total bill impact, based on 2-year and 4-year rate riders was estimated to be 12.5% and 10.6% respectively.

In its Argument-in-Chief however, Parry Sound Power proposed to recover the deferral and variance account balances over a 4-year period (and, also to recover the LRAM/SSM amounts over a 2 year period). Parry Sound Power made some additional revisions to its original application, reducing certain other costs, and revised the rate impact based on 4-year disposition to 9.67% for the 800 kWh residential customer. As this impact is now below the customary 10% bill impact mitigation threshold, and considering that Board staff has made a number of submissions which would work to reduce this impact further, staff has no further submissions on the bill impacts of this application.

IMPLEMENTATION

Parry Sound Power filed its application on October 15, 2010 for rates effective May 1, 2011. This is about 2 months later than expected, for new rates to have been approved and ordered by the Board in time for a May 1, 2011 implementation. In response to Parry Sound Power's request, the Board declared the current rates interim, effective May 1, 2011 on April 26, 2011.

In Parry Sound Power's Argument-in-Chief, the Applicant indicated that it "…requests the recovery of incremental revenue from May 1, 2011 until a decision and order is issued an effective."

Board staff submits that accounting for the two month late filing, the Board may wish to consider retroactive recovery of incremental revenues only if approval of the final rate order finalizes an effective date after July 1, 2011.

-All of which is respectfully submitted-