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BY EMAIL

February 1, 2008

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

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

**Re: Middlesex Power Distribution Corporation
2008 Incentive Regulation Mechanism Rate Application
Board File Number EB-2007-0867**

Please find attached Board staff's submission for the above proceeding for distribution to the applicant and any intervenors.

Yours truly,

Original signed by

Alexandre Ruest
Policy Advisor, Regulatory Policy Development

Encl.



ONTARIO ENERGY BOARD

STAFF SUBMISSION

2008 ELECTRICITY DISTRIBUTION RATES

Middlesex Power Distribution Corporation

EB-2007-0867

February 1, 2008

INTRODUCTION

On November 1, 2007, Middlesex Power Distribution Corporation (“Middlesex”) submitted an application based on the 2008 Incentive Regulation Mechanism (IRM) seeking approval for changes to the rates that Middlesex charges for electricity distribution, to be effective May 1, 2008. Middlesex’s application also requested approval for new smart meter rate adders. The purpose of this document is to provide the Ontario Energy Board (the “Board”) with the submissions of Board staff after its review of the evidence submitted by Middlesex.

SMART METER

Background

In the 2006 rate setting proceedings, a number of distributors indicated that they might have difficulty implementing the announced smart meter installations targets without financial assistance. To address this need, the Board provided advanced funding in the form of a smart meter rate adder in the years before rebasing. However, the Board indicated that rate adders are not set to guarantee costs recovery, nor are they set at a level that is deemed to be prudent. This prudence review is undertaken at a later date, as explained below. As well as providing advance funding, rate adders phase in the rate increase that could otherwise arise if the cost of the smart meters were brought into rate base all at once in a future year. Rate adders are to be removed once smart meter asset balances are included in approved rate base and their costs incorporated into a re-based revenue requirement.

Following its Decision on certain generic 2006 EDR issues, the Board also established variance accounts to capture the amounts recovered through the rate adders and the revenue requirement associated with smart meters. Once a prudence review has been conducted by the Board, the net amounts accumulated in the variance accounts are disposed of through a rate rider. In the intervening period between the expiry date of the rate rider and the time of re-basing, the revenue requirement associated with these

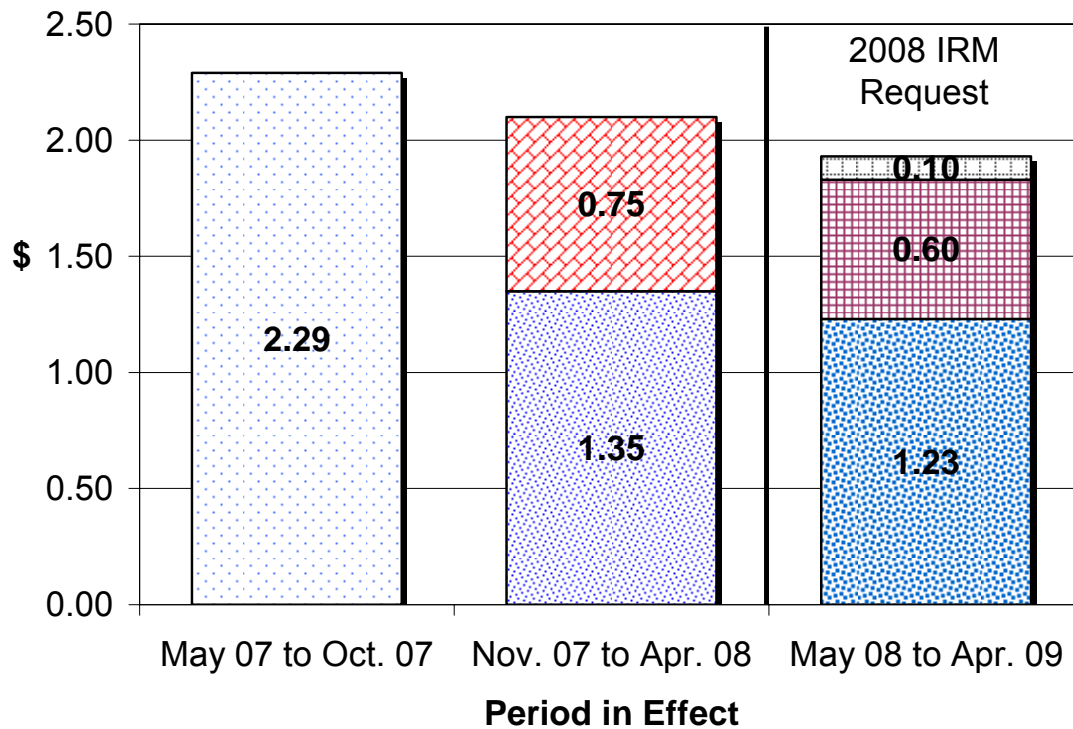
Board approved smart metering costs is captured in a new rate adder (permanent capital adjustment). Upon re-basing, a typical approach would be to include approved smart meter expenditures in rate base and the revenue requirement adjusted accordingly. The rate adder would then not be necessary.

Middlesex is one of the licensed distributors authorized by Ontario Regulation 427/06 to conduct discretionary metering activities. In its EB-2007-0553 and EB-2007-0110 Decision and Order dated April 20, 2007, the Board approved Middlesex's request for a smart meter rate adder of \$2.29 per metered customer per month (MC/month) effective May 1, 2007. Following the EB-2007-0063 and EB-2007-0553 Rate Order dated October 26, 2007, the Board approved a one –year rate rider of \$0.75/MC/month to dispose of the variance between the amounts recovered through the rate adder up to October 31, 2007, and the Board approved smart metering costs up to April 30, 2007. A new rate adder of \$1.35/MC/month was also implemented effective November 1, 2007, to fund planned smart meter installations from May 1 to December 31, 2007.

Middlesex is now applying to recover through a rate adder (permanent capital adjustment) the 2008 revenue requirement associated with the Board approved smart metering costs up to April 30, 2007. This proposed rate adder amounts to \$1.23/MC/month and would be effective over the 2008 rate year. Middlesex also proposes, effective May 1, 2008, the establishment of two new one-year rate adders totalling \$0.70/MC/month (\$0.60/MC/month related to residential installations made between May 1, 2007, and December 31, 2007, and \$0.10/MC/month associated with general service installation made up to September 30, 2007). If approved, Middlesex's total monthly service charge for smart meters would decrease to \$1.93/MC/month from the current \$2.10/MC/month. Figure 1 on the next page depicts the elements described above.

Staff notes that Middlesex has reflected in its application the termination, effective May 1, 2008, of the existing \$0.75/MC/month rate rider and the \$1.35/MC/month rate adder.

**Figure 1: Monthly Smart Meter Charge
 per Metered Customer**



Rate Rider

- ☒ True-up of residential costs approved up to Apr. 07

Rate Adder

- ☐ Funding for first part of planned 2007 Installations
- ☐ Funding for remainder of planned 2007 installations
- ☐ Proposed for general service installations made up to Sept. 07
- ☐ Proposed for residential installations made between May 07 and Dec. 07
- ☐ Proposed permanent capital adjustment for installations made up to Apr. 07

Discussion and Submission

New rate adder (permanent capital adjustment) of \$1.23/MC/month

Staff notes that the proposed rate adder of \$1.23/MC/month was calculated using the Board computer model filed by Middlesex in the EB-2007-0063 and EB-2007-0553 proceeding, and is meant to recover the 2008 revenue requirement associated with the Board approved smart metering costs up to April 30, 2007.

In its Decision with Reasons for EB-2007-0063, the Board stated that:

“For those applicants that are not part of the first tranche of cost of service applications, the incentive rate mechanism process will recognize the costs approved in this Decision. This will allow distributors to include costs related to minimum functionality, as approved in this Decision, in their incentive rate adjustment.”

If the Board approves the \$1.23/MC/month rate adder submitted by Middlesex, it is staff's understanding that monies collected through this rate would be a return on and of capital for the capital expenditures approved in EB-2007-0063. As such, it is Board staff's understanding that these monies would not be recorded in a variance account.

New Rate Adder of \$0.60/MC/month

Middlesex is applying for two new one-year rate adders: one for residential smart meters installed between May 1, 2007, and December 31, 2007, (\$0.60/MC/month); and the other for smart meters installed up to the September 30, 2007, for general service customers with a demand less than 50 kW and general service customer with a demand greater than 50 kW (\$0.10/MC/month). Those rate adders were calculated using the computer model used in the EB-2007-0063 and EB-2007-0553 proceeding.

Through an interrogatory response, Middlesex clarified that it is not asking that a prudence review of the costs underpinning the calculation of the proposed new rate adders be conducted in this proceeding. Staff understands that Middlesex intends to “apply for final recovery of costs incurred for all installed meters at April 30, 2008,” at a later date.

Board staff notes that the funding that Middlesex is requesting with regard to the installation of residential smart meters (i.e., the \$0.60/MC/month rate adder) has already been provided through the \$1.35/MC/month rate adder that became effective on November 1, 2007. Staff's understanding is based on the fact that the amounts and smart meter installation projections used for the calculation of both the \$1.35/MC/month rate adder and the requested \$0.60/MC/month rate adder are the same, except for the exclusion of \$6,250 in incremental operating spending in Middlesex's proposed \$0.60/MC/month rate adder. In addition, the model identifies these amounts as pertaining to 2007 rather than calculating the revenue requirement on these installations for 2008. Board staff asks Middlesex to confirm this point. Nonetheless, this does not change staff's observation below.

The applicant is asked to comment on whether the Board should consider maintaining the existing \$1.35/MC/month rate adder in place for the 2008 rate year since Middlesex has not requested in its application any amount for a 2008 return on and of capital for the residential smart meter installations made between May 1, 2007, and December 31, 2007. While those expenses have not been approved yet, the applicant is asked to comment on whether it is appropriate, for rate stability, to provide relief for their associated costs up until a decision is made on those installations. The continuation of the \$1.35/MC/month rate adder would provide continued funding for Middlesex's smart meter program, which will be subject to a prudence review in a later proceeding.

Staff notes that the existing \$1.35/MC/month rate adder is comparable to the proposed rate adder of \$1.23/MC/month (permanent capital adjustment). The former relates to the installation of 2,937 residential smart meters while the latter relates to 3,063 residential installations. Moreover, Middlesex did not request any funding for their planned 2008 installation of 34 smart meters for customers with a demand less than 50 kW and 86 smart meters for customers with a demand greater than 50 kW. The \$1.35/MC/month rate adder could also be seen as providing funding for some or all of those activities.

New Rate Adder of \$0.10/MC/month

With regard to the \$0.10/MC/month rate adder, Middlesex stated in response to a Board staff interrogatory that the costs associated with it are within minimum functionality set out in Ontario Regulation 425/06. Board staff notes that Ontario Regulation 425/06 prescribes the criteria and requirements for meters for “residential and small general service consumers” to be those specified in the document entitled “Functional Specification for An Advanced Metering Infrastructure — Version 2.” That document states that “This Specification sets the required minimum level of functionality for AMI in the Province of Ontario for residential and small general service consumers where the metering of demand is not required.” Board staff notes that the only customer classes where the metering of demand is not required are the Residential class and the General Service Less Than 50 kW class. As part of the \$0.10/MC/month rate adder requested, Middlesex is seeking funding for smart meters installed for the General Service Greater Than 50 kW class.

Board staff also notes that in EB-2007-0063, Toronto Hydro-Electric System Limited agreed that the meters for 560 general service customers exceeded the minimum functionality in that these meters were to be used for billing of demand. The Board stated that it explicitly did not find “that the costs associated with these meters fall into the minimum functionality costs.” Nonetheless, the Board determined that those costs could be recovered, but that the approval of these costs was “ancillary to the smart meter decision.”

Board staff notes that the funding sought through the one-year \$0.10/MC/month rate adder totals \$8,083 and relates to a return equivalent to a return on rate base for installations made up to September 2007: 179 smart meters for General Service Less Than 50 kW customers and 47 smart meters for General Service Greater Than 50 kW customers.

RETAIL TRANSMISSION SERVICE RATES ADJUSTMENT

Background

In its letter dated October 29, 2007, the Board directed each distributor to propose an adjustment to their retail transmission rates (RTR) and disposition of the associated variance account balances in its 2008 Cost of Service or Incentive Rate Mechanism application, as applicable.

Middlesex proposes to reduce its RTR — Network Service Rate by 18.6% and its RTR — Line and Transformation Connection Service Rate by 12.6% for all its rate classes.

Discussion and Submission

To derive their proposed RTR adjustments, Middlesex determined their annual wholesale transmission network and connection costs based on the Board rate order dated October 17, 2007 (EB-2007-0759) and for 2006. These adjusted wholesale transmission network and connection costs were subsequently compared to revenue generated through existing retail transmission rates for the 2006 calendar year period to determine cost/revenue ratios for network and connection. The calculated cost/revenue ratios for network and connection were then applied to existing retail network and connection rates to derive the proposed adjustments to the RTR — Network Service Rate and RTR — Line and Transformation Connection Service Rate.

While Middlesex is partly embedded within Hydro One Networks Inc. (“Hydro One”), Middlesex assumed for the purpose of the derivation of the RTR adjustments that Hydro One, as a host distributor, will be charging rates equivalent to the new wholesale transmission rates.

All of which is respectfully submitted.