



December 15, 2011

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

**RE: 2012 ELECTRICITY DISTRIBUTION RATE APPLICATION FOR ALGOMA POWER INC.
("API") – EB-2011-0152
REPLY SUBMISSION**

Please find accompanying this letter two (2) copies of API's Reply Submission in the above captioned matter. Coincidentally with this written submission, a PDF version has been filed via the Board's Regulatory Electronic Submission System.

If you have any questions in connection with the above matter, please do not hesitate to contact the undersigned at (905) 994-3634.

Yours truly,

Original signed by:

Douglas R. Bradbury
Director, Regulatory Affairs

Enclosures

Algoma Power Inc.
Application for 2012 Electricity Distribution Rates
EB-2011-0152
Reply Submission

Introduction

Algoma Power Inc. ("API") filed an application with the Ontario Energy Board (the "Board") on September 15, 2011, under section 78 of the *Ontario Energy Board Act, 1998*, seeking approval for changes to the distribution rates that Algoma charges for electricity distribution, to be effective January 1, 2012. Algoma subsequently filed an amended application on October 13, 2011.

The purpose of this document is to provide the Board with API's reply to the submissions of Board staff and the Vulnerable Energy Consumers Coalition ("VECC").

1 Incentive Rate Regulation Mechanism and Remote and Rural Rate Protection

- 1.1 In its submission, Board staff asked that API confirm in its Reply Submission that it accepts this premise that the calculation of the price cap index as described in the Filing Requirements (price cap index = the change in annual GDP-IP less a productivity factor of 0.72 % and less a stretch factor).
- 1.2 API confirms this premise and that the proper productivity factor in the determination of the price cap index is 0.72%.

2 Price Cap Index

- 2.1 As discussed in part 1.1, API confirms that 0.72% is the correct productivity factor in the determination of the price cap index. API will use a productivity factor of 0.72% in its future calculations.
- 2.2 In their respective submissions, both Board staff and VECC noted that the Board issued a letter to all Licensed Electricity Distributors dated December 1, 2011 referencing "Board Determination of Stretch Factor Rankings for 2012 3rd Generation Incentive Regulation Applications (IRM3)". The stretch factor assigned to API is 0.6%.
- 2.3 Board staff and VECC have submitted that API ought to utilize a stretch factor of

0.6% pursuant to the Board's letter.

- 2.4 Board staff submitted that this 2012 Rate Application is not the appropriate venue for API to raise issues pertaining to the Board's separate determination as to which stretch factor applies; API disagrees with this assertion. Until this Application, API (or its predecessor) has never filed or has been required to file an incentive based rate application; the stretch factor was not a relevant measure in the determination of rates at API. Arising from API's last cost of service application, EB-2009-0278, API agreed to consult with the intervenors of record to develop and propose a form of incentive regulation that would accommodate API's unique circumstance. It is this development and proposal that gives rise to the use of a stretch factor in the determination of API's distribution rates and is therefore the proper forum for API to raise issues pertaining to the appropriate stretch factor.
- 2.5 Board staff goes on to assert that the reference in the EB-2007-0744 Decision to API's service area as "high cost" and "low revenue" does not support API's conclusion that a stretch factor based on a comparison of operating costs per customer is not suitable for API. Board staff has acknowledged that the Board took notice of the size of the service territory, the large asset base and low customer density as the basis for which Rural and Remote Rate Protection ("RRRP") was the non-traditional but appropriate rate-making response in the circumstances. Board staff then stated that it is not apparent to Board staff that there is a linkage, as claimed by API, between the circumstances which prompted the introduction of RRRP to mitigate what otherwise could be viewed as unreasonable rates and a separate fact-based determination of a particular utility's productivity ranking.
- 2.6 API submits that with a service territory so vast, its asset base so large and its customer density so low as to warrant RRRP funding to mitigate what otherwise could be viewed as unreasonable rates that a separate fact-based determination of API's particular productivity ranking is warranted. API's OM&A costs are a direct function of the staff, equipment and resources that are required to effectively operate a distribution system spanning such a vast service territory and maintain the large asset base. OM&A costs are a direct link to what otherwise could be viewed as unreasonable rates and has warranted the unusual introduction of RRRP to mitigate rates.
- 2.7 Finally, Board staff has submitted that if API viewed the stretch factor methodology as inappropriate because of its special circumstances, then the onus was on API (or its predecessor) to make its position and concerns known so that they could be properly considered by the Board. Therefore API's failure to communicate its concerns to the Board, because it did not believe that IRM based rate making would apply to it, is not a justifiable basis for applying a stretch factor different than that communicated by the Board. API disagrees, arising from the Board's decision in EB-2009-0278, API and the intervenors of record agreed to consult to develop and propose a form of incentive regulation that would accommodate API's unique circumstance. It is in this venue that the appropriate stretch factor applicable to API

ought to be determined given the unique nature of API's rate setting regime.

- 2.8 API submits that its well established recognition as a "high cost" and "low revenue" distributor with a vast service territory, the large asset base and low customer density means that it does not have a peer within the peer groups of Ontario LDCs. API's service area is more than twice the area of the greater Toronto area. It has less than 12,000 customers and has the lowest customer/kilometer ratio in Ontario with only 6.7 customers per kilometer on average. 99.9% of its service area is rugged and sparsely populated wilderness. Its service area is characterized by long runs of distribution wire between customers.¹
- 2.9 API further submits that the only just and reasonable stretch factor applicable API, in the absence of further fact based metrics, is the midpoint, 0.4%. The midpoint represents a reasonable proxy for a licenced distributor that has very little control over the OM&A costs associated with factors out of its control such as: a vast service territory, rugged geography, low customer density, and remoteness. All of which are considerations in the methodology for the application of RRRP.

3 RRRP Adjustment Factor

- 3.1 By way of letter dated December 7, 2011, the Board indicated that the RRRP adjustment factor to be utilized in the setting of 2012 rates is 2.81%.
- 3.2 API will use a RRRP Adjustment Factor of 2.81% in its future calculations.

4 Revenue to Cost Ratio

- 4.1 Both Board staff and VECC submitted that the Board should deny the adjustments to the Revenue to Cost ratios proposed by API on the basis that the Filing Requirements, at page 24, state that "...changes to revenue-to-cost ratios, other than pursuant to a prior Board decision" are to be excluded from the IRM application process.
- 4.2 API has acknowledged that the Board's decision in the matter of EB-2009-0278 did not order future year changes to the approved revenue to cost ratios and is prepared to accept denial of the proposed adjustments on that basis (only).
- 4.3 Board staff in its submission went on to state, *"In the event that the Board determines that changes to the Revenue to Cost ratios are appropriate in this proceeding, Board staff wishes to note the following. In the methodology proposed by Algoma, changes in the Revenue to Cost ratios that affect the R-1 and R-2 customer classes have an impact on the amount of revenue requirement that will be funded in 2012 by RRRP. This results because the RRRP adjustment (average*

¹ Board Decision and Order, EB-2007-0744, page 3, October 30, 2008

province-wide change in rates) is applied to the post RRRP rates approved in 2011 while the proposed 2012 revenue requirement for each customer class reflects the changes in Revenue to Cost ratios. All else equal this will impact the level of RRRP funding and, depending on the direction of the Revenue to Cost ratio changes, the customers in the rest of the province will be thereby affected.”

- 4.4 API cannot accept this position presented by Board staff. API views this as a value judgment in which Board staff deems it to be more important to protect the rates of the customers in the rest of the province at the expense of the Seasonal customers at API.
- 4.5 Determination of class specific revenue to cost ratios and calculation of the fixed and variable charges made following the determination of a revenue to cost ratio are distinct and separate exercises; especially so at API in light of O. Reg. 442/01.
- 4.6 The Board placed a letter from J. Reid Duncan, dated November 1, 2011, on the file for EB-2011-0152, in which among other matters expresses concerns related to the rate for seasonal customers in API. Similar views have been represented to the Board by other parties but do not form part of this proceeding.
- 4.7 Under the most recent Board approved revenue to cost ratios, EB-2009-0278, Seasonal customers, who do not enjoy the benefit of the RRRP, have a revenue to cost ratio of 115%. Residential R2 customers, who do enjoy the benefits of RRRP, have a revenue to cost ratio of 59.8%. On the basis of the Board staff submission on this matter, API would not be able to reduce the revenue to cost ratio of the Seasonal class because it would mean that revenue recovery is shifted to a customer class that is subject to RRRP funding and indirectly will impact the Rural Rate Protection service charge to the electricity distribution customers in the rest of the province.
- 4.8 API submits that in the event that the Board denies the changes in revenue to cost ratio proposed by API that it do so pursuant to its decision in EB-2009-0278 and clearly not because a change in revenue to cost ratios that afford rate relief to API's Seasonal customer class may increase the RRRP funding requirement for 2012.

5 Federal and Provincial Income Taxes

- 5.1 Board staff has submitted that API's calculation of the 2012 tax savings is inappropriate. API utilized a combined (Federal/ Provincial) tax rate of 26.25% for 2012 to calculate the 2012 tax savings, amounting to \$47,983 to be shared with ratepayers. Board staff asserts that the API 2012 tax savings determination does not reflect the Ontario Small Business Deduction ("OSBD"). If the OSBD calculation is included, the amount of tax savings to be shared would be \$107,897.
- 5.2 In response to a Board staff interrogatory, API stated that it is not eligible for the OSBD. API is not a Canadian-controlled Private Corporation as it is owned indirectly

by a public corporation and this does not qualify it for the OSBD. API will pay income tax in 2012 at the rate of 26.25%

- 5.3 To support its submission, Board staff notes that API's predecessor company, Great Lakes Power Limited ("GLPL"), filed its most recent rates application, EB-2007-0744, on a stand-alone basis for the distribution business, even though GLPL also carried on other activities. While GLPL as a whole was 100% equity financed, the debt and equity of the distribution business was quantified on a stand-alone basis and taxes were calculated on that basis. The Board approved the stand-alone approach as the basis for setting GLPL's rates, including the calculation of taxes. Board staff does not believe that a change in ownership should result in discontinuation of the stand alone principle. Board staff submits that the tax calculation to determine the amount of tax savings to be shared with customers should treat API as if it were a stand-alone distribution company and therefore the amount to be shared should be \$107,897.
- 5.4 API strongly disagrees with the Board staff submission on this matter.
- 5.5 Board staff supports its submission on the basis of an application by Great Lakes Power Limited, EB-2007-0744, pre-dating API. Board staff fails to discuss or acknowledge in any manner, EB-2009-0278, a more recent cost of service application by API to set just and reasonable electricity distribution rates. The Board issued its Decision and Order in the matter of EB-2009-0278 in January of 2011 with rates effective December 2010.
- 5.6 API, in the matter of EB-2009-0278, presented evidence supporting its Federal and Provincial Income Taxes included in its 2011 revenue requirement. This evidence was open to review by intervenors and Board staff in an extensive series of written interrogatories and oral examination.
- 5.7 The amount of Federal and Provincial Income Taxes included in API Board Approved 2011 revenue requirement was determined on the basis of combined (Federal/ Provincial) tax rate of 28.25%. This is shown in the 2012 Tax Savings Workform provided as part of this API 2012 Distribution Rate Application. API applied the same methodology to calculate the 2012 shared tax savings with a combined (Federal/ Provincial) tax rate of 26.25%. A shared tax savings of \$47,983.
- 5.8 The Board staff submission in this matter is akin to amending the Board's final decision in EB-2009-0278. Board staff is asserting that the amount of Federal and Provincial Income Taxes and the methodology to determine those taxes included in the API Board Approved 2011 revenue requirement is, in their opinion, wrong. To correct this assumed error, Board staff are proposing to modify the manner in which API determines its Federal and Provincial Income Taxes during an incentive based adjustment to rates.
- 5.9 The Board's updated Chapter 3 of the Filing Requirements for Transmission and Distribution Applications dated June 22, 2011 provides guidance on matters that ought to be included in an incentive based application. The guidelines indicate that

the process is intended to streamline the processing of a large volume of rate adjustment applications, and is therefore mechanistic in nature. For this reason, the Board has determined that the process is not the appropriate venue by which a distributor should seek relief on issues which are substantially unique to an individual distributor or more complicated and potentially contentious.

- 5.10 In their respective submission, both Board staff² and VECC³ have drawn reference to Chapter 3 of the Filing Requirements and particularly Section 4.0, Specific Exclusions from IRM Applications. API submits that the guidance provided in Chapter 3 of the Filing Requirements for Transmission and Distribution Applications dated June 22, 2011 ought to apply in this matter as submitted by Board staff. The matter of the proper combined Federal and Provincial Tax Rate is unique to the API is more complicated and potentially contentious and ought not to be decided in the absence of an evidentiary review.
- 5.11 API submits that the Board ought to approve the 2012 tax savings of \$47,983 to be shared with ratepayers as contained in the API Application. That savings is based on the same methodology applied in EB-2009-0278 that was accepted by the Board in a final decision. This incentive based application builds on the rates and methodologies from the final decision in EB-2009-0278.
- 5.12 Further, API submits that the Board Staff proposal that API's tax savings would be higher if it were a stand-alone utility, and therefore API's ratepayers should receive the benefit of those assumed increased savings is incorrect. This application of the stand alone principle extends its purpose to penalizing utilities that do not operate on a stand-alone basis or are not owned by a municipality.
- API's actual 2012 tax savings will be \$47,983. To assume fictitious tax savings of \$107,897 as suggested by Board Staff will penalize API for not-being a stand-alone utility. API's actual tax savings will not be \$107,897, so it would have to make up the difference between \$47,983 and \$107,897, amounting to a \$59,914 penalty.
- 5.13 For all of these reasons, API submits that Board Staff's position on this issue should be rejected.

6 Smart Meters

- 6.1 In its submission Board staff has agreed with API's request to add an April 30, 2012 sunset date to the SMFA that will continue in the proposed rates for 2012.
- 6.2 API agrees with the Board staff submission in this matter.

² Board staff Submission, December 8, 2011, page 7,

³ VECC Submission, December 8, 2011, paragraph 2.2

7 Retail Transmission Service Rates (“RTSR”) Adjustment

- 7.1 In their submission, Board staff asked API, in its submission, to identify, and if necessary, correct any misstatements in the tables at the top of page 10. API confirms that the values contained in these tables correctly reflect the evidence.
- 7.2 Board staff has stated in its submission that it questions API’s argument that it is inappropriate to use the RTSR Workform to calculate the 2012 RTSRs because the 2011 UTRs were unavailable when the existing RSTRs were set. This is NOT a correct interpretation of API’s argument.
- 7.3 In API’s last cost of service application, EB-2009-0278, API utilized a historical review of its wholesale transmission costs and historical RTSR revenues. This review was the same as is performed in the RTSR Workform. Arising from this review, API calculated a correction factor to align future RTSRs with projected wholesale transmission costs taking into account the known increases in the UTRs. This is the same process that the RTSR Workform performs.
- 7.4 Arising from this review of its wholesale transmission costs and historical RTSR revenues, API proposed new RTSRs in EB-2009-0278. The proposed RTSRs were Board approved in January 2011 and made effective on December 1, 2010.
- 7.5 Since API’s updated RTSRs were not made effective until December 2010, the 2010 twelve month review of wholesale transmission costs and historical RTSR revenues as performed in the 2012 RTSR Workform will not recognize the historical correction factor embedded within the current Board Approved RTSRs. Parties will require the 2011 analysis of wholesale transmission costs and RTSR revenue to know if the correction factors introduced in December 2010 are working.
- 7.6 If API uses the 2010 data set in the 2012 RTSR Workform, as submitted by Board staff, API will be analyzing the same trending of wholesale transmission costs and historical RTSR revenues as was performed in EB-2009-0278 and any correction factor arising from the Workform will be compounded with that already used to set the RTSR rates which became effective in December 2010.
- 7.7 Compounding the RTSR correction made in EB-2009-0278 with another using 2010 data in the 2012 RTSR Workform will unnecessarily increase RTSRs for API’s electricity distribution customers.
- 7.8 API submits that the appropriate adjustment to RTSRs is to index the current Board Approved RTSRs with known changes in the UTRs.
- 7.9 API submits that the Board ought to approve the RTSRs proposed by API in its Application.

8 Disposition of Deferral and Variance Accounts as per the Electricity Distributors' Deferral and variance Account Review Report (the "EDDVAR Report")

- 8.1 Board staff submitted that it accepts that the revised amounts are in accordance with the findings of the regulatory audit and on this basis; Board staff accepts them as filed. Board staff has reviewed the associated rate rider calculations, including the charge determinants and term. The charge determinants and term are unchanged as compared to what was previously filed. Board staff submits that the revised rate riders should be accepted by the Board.
- 8.2 API agrees with the Board staff submission in this matter.
- 8.3 In the Proposed Revised Settlement Agreement dated September 17, 2010, item No. 9a settled the disposition of select deferral and variance accounts. The parties agreed to dispose of RSVA Power excluding Global Adjustment, account 1588. It has now been determined that due to an oversight in the preparation and submission of the Draft Rate Order that the RSVA Power Global Adjustment subaccount was in fact disposed. The amount of the disposition including interest was \$66,872 payable to the customer. This amount was included with the remainder of the Group 1 Deferral and Variance Account disposition and allocated on kWh.
- 8.4 API submits that the current Rate Rider for Deferral/Variance Account Disposition – effective until December 31, 2011 which is settling this balance be allowed to run its term. In a future proceeding, when API has the capacity to dispose of Global Adjustment through a separate rate rider, this balance may be reconciled and settled as per Board direction. API expects to have the capacity to dispose of Global Adjustment through a separate rate rider at January 1, 2013.

9 Account 1562 (Deferred Payments in Lieu of Taxes)

- 9.1 Board staff has submitted that pursuant to the direction provided by the Board to certain other 2012 IRM filers, API should file a stand-alone application to dispose of account 1562 by April 1, 2012.
- 9.2 API agrees with the Board staff submission in this matter.

10 Account 1521 – Special Purpose Charge ("SPC")

- 10.1 Board staff noted that it is API's intention to file for disposition of the account balances by April 15, 2012 and expressed no other concerns.
- 10.2 API agrees with the Board staff submission in this matter.

11 General Update

11.1 Board staff submitted that in order to facilitate the issuance of a timely rate order, API should consider filing with its reply submission a scenario whereby its final rates are calculated using the following values:

- The RRRP adjustment of 2.81%;
- The % change in the GDP-IPI (Price Escalator) of 1.7%;
- The Stretch Factor of 0.6%;
- The Productivity Factor of 0.72%;
- No change to the revenue to cost ratios;
- The revised deferral and variance account balance and proposed disposition period;
- The tax sharing amount of \$107,897;and
- Revised retail transmission rates based on the RTSR Workform methodology.

11.2 API submits that as a result of the unsettled nature of many of the preceding matters it would be premature at this time to submit a scenario whereby its final rates have been calculated.

All of Which Is Respectfully Submitted