Ontario Energy Board
P.O. Box 2319
27th. Floor
2300 Yonge Street
Toronto ON M4P 1E4
Telephone: 416-481-1967
Facsimile: 416-440-7656
Toll free: 1-888-632-6273

Commission de l'énergie de l'Ontario
C.P. 2319
27e étage
2300, rue Yonge
Toronto ON M4P 1E4
Téléphone; 416-481-1967
Télécopieur: 416-440-7656
Numéro sans frais: 1-888-632-6273

Ontario

BY EMAIL

January 9, 2012

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

Dear Ms. Walli:

Re: North Bay Hydro Distribution Ltd. ("North Bay")
2012 IRM3 Distribution Rate Application
Board Staff Submission
Board File No. EB-2011-0187

In accordance with the Notice of Application and Hearing, please find attached the Board Staff Submission in the above proceeding. Please forward the following to North Bay Hydro Distribution Ltd. and to all other registered parties to this proceeding.

In addition please remind North Bay Hydro Distribution Ltd. that its Reply Submission is due by January 23, 2012.

Yours truly,

Original Signed By

Christiane Wong
Information Administrator, Applications & Regulatory Audit

Encl.

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2012 ELECTRICITY DISTRIBUTION RATES

North Bay Hydro Distribution Ltd.

EB-2011-0187

January 9, 2012

Board Staff Submission
North Bay Hydro Distribution Ltd.
2012 IRM3 Rate Application
EB-2011-0187

<u>Introduction</u>

North Bay Hydro Distribution Ltd. ("North Bay") filed an application (the "Application") with the Ontario Energy Board (the "Board"), received on October 14, 2011, under section 78 of the *Ontario Energy Board Act, 1998*, seeking approval for changes to the distribution rates that North Bay charges for electricity distribution, to be effective May 1, 2012. The Application is based on the 2011 3rd Generation Incentive Regulation Mechanism.

The purpose of this document is to provide the Board with the submissions of Board staff based on its review of the evidence submitted by North Bay.

In the interrogatory phase, Board staff identified certain discrepancies in the data entered in the application models by North Bay. In response to Board staff interrogatories which requested either a confirmation that these discrepancies were errors or an explanation supporting the validity of the original data filed with the application, North Bay confirmed certain errors as described below and provided the necessary corrections to the models.

Staff notes that North Bay is proposing to maintain its smart grid funding adder of $0.08 per metered customer per month as previously approved by the Board. North Bay stated that the Board in its 2010 Cost of Service Decision (EB-2009-0270) approved this funding adder through the IRM period.

Board staff makes submissions on the following matters:

- Adjustments to the Revenue-to-Cost Ratios;
- Disposition of Group 1 Deferral and Variance Account Balances;
- Account 1562 – PILs Disposition;
- Account 1521 – Special Purpose Charge ("SPC");;
- Shared Tax Savings; and
- Lost Revenue Adjustment Mechanism ("LRAM").

ADJUSTMENTS TO THE REVENUE-TO-COST-RATIOS

Background

As approved in its 2010 cost of service application (EB-2009-0270), North Bay adjusted the revenue-to cost ratios for the Street Lighting, Sentinel Lighting and the General Service >3,000 to 4,999 kW rate classes to the bottom of the corresponding Board approved target range. The incremental revenues from these customer rate classes was used to reduce the revenue-to-cost ratios for the GS<50 kW and GS > 50 kW rate classes.

Submission

Board staff submits that the proposed revenue-to-cost ratio adjustments are in accordance with the Board's Decision in the EB-2009-0270 proceeding.

DISPOSITION OF GROUP 1 DEFERRAL AND VARIANCE ACCOUNT BALANCES

Background

The *Report of the Board on Electricity Distributors' Deferral and Variance Account Review Initiative (the "*EDDVAR Report") provides that during the IRM plan term, the distributor's Group 1 audited account balances will be reviewed and disposed if the preset disposition threshold of $0.001 per kWh (debit or credit) is exceeded.

North Bay completed the 2012 IRM Rate Generator. The 2010 actual year end amount for Group 1 accounts with interest projected to April 30, 2012 is a debit of $753,759. Debit balances are amounts recoverable from customers. This amount results in a total claim of $0.00134 per kWh which exceeds the preset disposition threshold of $0.001 per kWh.

In response to Board staff interrogatory #2, North Bay confirmed that the balance in Account 1588 is composed of a credit amount of $55,288 RSVA Power (excluding Global Adjustment) and a debit amount of $567,580 RSVA Power Sub-Account – Global Adjustment.

North Bay did not previously have the billing capability to dispose of the global adjustment sub-account by means of a separate rate rider that would prospectively apply to non-RPP customer only. In North Bay's 2011 IRM Decision and Order, the Board stated its expectation that North Bay Hydro will be in a position to dispose of the global adjustment sub-account by means of a separate rate rider applied only to Non-RPP customers as soon as possible, and no later than at the time of its next rebasing. In this current application, North Bay indicated that they will be able to do so effective May 1, 2012.

North Bay proposed a two-year disposition period for its Group 1 account balances, rather than the default disposition period of one-year. North Bay stated that the default disposition used to clear Account balances through a rate rider should be one year, however, with the inclusion of the LRAM claim, Account 1562 and the large debit balance in Account 1588 Global Adjustment Sub-Account, phasing the disposition over a two-year period would mitigate the rate impacts and maintain the simplicity of the tariff sheet.

Submission

Board staff has reviewed North Bay's Group 1 Deferral and Variance account balances and notes that the principal amounts to be disposed of as of December 31, 2010 reconcile with the amounts reported as part of the RRR. Board staff therefore submits that the amounts should be disposed of on a final basis.

Board staff notes that North Bay's application is not consistent with the guidelines outlined in the EDDVAR Report with respect to the default disposition period for Group 1 accounts (i.e. one year). Staff notes that the total bill impact using a one year disposition period is an increase of 2.32% while the total bill impact for two years (as proposed) is an increase of 0.47%. These bill impacts include North Bay's Group1 account balances and accounts 1521 and 1562.

While recognizing the value of the EDDVAR Report in guiding decisions with respect to the disposition of deferral and variance account balances, Board staff notes that in the past, the Board has made decisions which deviate from the EDDVAR Report if it deems it in the public interest to do so. For example, in Guelph Hydro's 2010 IRM application (EB-2009-0226), Guelph Hydro requested to dispose of Group 1 Account balances over a four-year period citing that disposition over a one-year period would negatively impact its cash flows. In that proceeding, Board staff submitted that while some volatility in customer bills may occur, it was in the best interest of customers to dispose of account balances over a shorter time frame so as to reduce intergenerational inequity. The Board found that Guelph's rationale for proposing to extend the disposition was reasonable but believed that a four-year disposition period was too long. The Board found that a disposition period of two years was appropriate.

In this application, Board staff believes that using a disposition period of 2 years would strike an appropriate balance between reducing intergenerational inequity and mitigating rate volatility. Therefore, Board staff supports North Bay's proposed disposition period of two years.

Account 1562 – PILs Disposition

Background

Combined Proceeding (EB-2008-0381)

In 2001, the Board approved a regulatory PILs tax proxy approach for rate applications coupled with a true-up mechanism filed under the Reporting and Record-keeping Requirements ("RRR") to account for changes in tax legislation and rules, and to true-up between certain proxy amounts used to set rates and the actual amounts. The variances resulting from the true-up were tracked in account 1562 for the period 2001 through April 30, 2006.

On December 18, 2009 the Board issued a decision in the Combined PILs Proceeding (EB-2008-0381) and provided its views on how it will review the evidence related to account 1562 deferred PILs.

In that Decision, the Board states that:
"The parties may well differ in their interpretations of the methodology but the Board will decide those questions on the basis of the facts and the underlying documents. The Board will not enter into an enquiry as to what the methodology should have been but rather, will determine, where necessary, what the methodology was and what the appropriate application of the methodology should have been".[1]

[1] EB-2008-0381Combined Proceeding, Account 1562 Deferred Payments in Lieu of Taxes (PILs), Decision with Reasons, December 18, 2009, pg. 7.

The PILs evidence filed by North Bay in this proceeding includes tax returns, financial statements, Excel models from prior applications, calculations of amounts recovered from customers, SIMPIL[2] Excel worksheets and continuity schedules that show the principal and interest amounts in the PILs 1562 account balance.

<u>Previous North Bay Applications (RP-2000-0213/EB-2000-0454)</u>

In North Bay's 2001 rate application, North Bay had proposed unbundled rates to be effective on the market opening date of May 1, 2002. Paragraph 4.2 on page 6 states:

> "The Company is not applying for rate changes at this time and proposes to maintain its existing rate structure until market opening or a cost allocation and rate design study, whichever comes first, to avoid rate impacts and to ensure all customers have been treated fairly and consistently."

Paragraph 4.4 on page 7 continues:

> "The Council of the City of North Bay has previously approved a sustainable profit model for North Bay Hydro with a target rate of return on equity of approximately 3 to 4% and is forgoing a dividend. The Board of Directors of North Bay Hydro Distribution Limited has endorsed the Council's approved return level of 3 to 4%. They further authorized the President of the Company to file the necessary applications with the OEB to maintain existing rate structures until market opening and for an order or orders approving just and reasonable rates for other charges effective 30 days after approval by the OEB."

North Bay voluntarily remained on a bundled rate structure until May 1, 2002 and in order to mitigate customer impact, North Bay voluntarily requested that the unbundled rate impact including the 2001 and 2002 PILs proxies not take effect until May 1, 2002. Accordingly, North Bay was not eligible to start collecting PILs from its customers until May 1, 2002.

Page 2 of the Amended Manager's Summary for North Bay's 2002 rate application states:

[2] Spreadsheet implementation model for payments-in-lieu of taxes

> "The increase of distribution revenues as a result of this rate submission is $1,247,835. This excludes about $690,000 in account 1570 for transition costs and a reduction of $740,854 in 2002 proxy taxes. We plan to recover the associated loss of revenue through efficiency improvements for both these amounts. If need be we will submit for Transition costs and proxy taxes during the next annual filing."

As indicated in the above excerpt, North Bay had fully expected to recover any loss in revenue through efficiency gains. Paragraph 5.9 on page 4 states:

> "We are confident in the financial viability of the utility and wish to lessen consumer impacts. The Shareholder, Utility and the Public all wish to limit rate increases."

Submission

2001 Fourth Quarter and 2002 PILs Entitlements

In interrogatories, Board staff asked why North Bay believed that its entitlement to the 2001 fourth quarter and 2002 PILs proxy should begin prior to May 1, 2002. North Bay's response was:

> "NBHDL, as with the majority of LDCs in the province, became taxable (via PILS) on October 1, 2001. Through the natural cycle of rate setting in the industry, distribution rates including recovery of PILS were not approved until May 1, 2002 (effective date).
>
> North Bay Hydro has replicated the schedule approved through the combined proceeding decision (EB-2008-0381). In the combined proceeding the applicants commenced the Q4 2001 entitlements in October 2001 and 2002 entitlements in January 2002."

The applicants in the Combined Proceeding had an effective date of rate change including the 2001 and 2002 PILs proxies on March 1, 2002. North Bay requested, and was granted, an effective date of rate change of May 1, 2002 so that, for the 2002 rate year, North Bay was only eligible to recover PILs in rates from May 1, 2002.

Board staff submits that since North Bay requested, and the Board granted an effective date of rate change of May 1, 2002, North Bay should not record the 2001 fourth quarter and 2002 PILs proxies or entitlements for the period prior to the effective date of May 1, 2002. Board staff submits that North Bay should file the revised PILs reconciliation worksheet, continuity schedule and EDDVAR continuity schedule.

Board staff submits that the proxy recognition in the continuity schedule should be based on the number of months between May 1, 2002 and the next rate change approved by the Board which will result in a lower proxy that reflects the number of months of collection from ratepayers.

Write-down of Capital Property and Loss of Disposal of Assets

Under the PILs methodology, Board staff submits that fixed asset transactions should not true-up to ratepayers and thus appear on the TAXREC3 sheet of the SIMPIL model. Utilities receive a return on fixed assets included in rate base and, if an asset is written down or disposed, the utility continues to receive a return until its next rate rebasing application.

In the 2002 tax year, North Bay reported on the tax return a write-down of capital property of $540,755. A write-down of assets is accelerated depreciation and Board staff submits that this should not true-up to ratepayers under the established Board methodology. This amount appears as an addition in the 2002 SIMPIL model TAXREC2 sheet row 34 cell C34. Material items recorded on TAXREC2 true-up to the ratepayers only.

In interrogatories, Board staff asked why North Bay believed that this asset write-down should true up to ratepayers and not the shareholder. North Bay's response was:

> "The write-down relates to the movement to fair market value of an asset that was, at the time, used by NBHDL to provide distribution services to its customers. Costs related to provision of distribution services are allowed to be recovered in rates.
>
> While NBHDL did not apply for specific recovery of the write-down it continued to receive payments from customers to partially mitigate the loss of economic value. NBHDL continued to receive, in the 2002 to 2006 period, depreciation and market

> based rate of return related to the write-down amount. This stopped in 2006 when LDCs were permitted to rebase for distribution rates May 1, 2006 based on December 31, 2004 values (which reflected the write-down).
>
> In addition, NBHDL through its treatment of the write-down as a TAXREC2 item resulting in true up from its customers is filing for recovery of the tax impact only related to the write-down. On a net basis the shareholder still absorbed a portion of the write-down.
>
> NBHDL considers this treatment fair as the asset was required for service and did not exist exclusively for the benefit of the shareholder."

From its response, North Bay has confirmed that from 2002 to 2006 shareholders continued to receive a benefit in distribution rates. In addition, North Bay had the opportunity to file an application to make an adjustment to its 2002 rate base. However, it chose not to file an application to reduce the fixed asset value in rate base. As such, North Bay continued to recover a higher return from these written down assets during the period 2002 to May 1, 2006.

In the 2004 tax year, this same asset was sold to a third party and North Bay recorded a loss on disposal of the asset of $144,597. This amount appears as an addition in the 2004 SIMPIL model TAXREC2 sheet row 19 cell C19. Material items recorded on TAXREC2 true-up to the ratepayers only.

In interrogatories, Board staff asked why North Bay believed that a loss on disposal of assets on which shareholders are getting a return in distribution rates and a CCA tax benefit should true up to ratepayers and not the shareholder. North Bay's response was:

> "NBHDL believes its treatment as a TAXREC2 item with true-up from its customers is fair for the same reasons articulated in response to question 7 d).
>
> NBHDL sold the facility in 2004 as part of an effort to rationalize facilities and ultimately reduce costs for customers. NBHDL did not apply for specific recovery of the loss on sale. Again, NBHDL continued to receive payments from customers to partially mitigate the loss on sale. NBHDL continued to receive, in the 2004 to

> 2006 period, depreciation and market based rate of return related to the loss on disposal amount. This stopped in 2006 when LDCs were permitted to rebase for distribution rates May 1, 2006 based on based on December 31, 2004 values (reflected the sale).
>
> NBHDL through its treatment of the loss on disposal as a TAXREC2 item resulting in true up from its customers is filing for recovery of the tax impact only related to the loss. On a net basis the shareholder still absorbed a portion of the loss on disposal (a larger portion than the write-down to FMV).
>
> NBHDL considers this treatment to be fair as the loss on sale led to future reduced costs for customers and the asset did not exist exclusively for the benefit of the shareholder."

In the response excerpted above, North Bay has confirmed that shareholders continued to receive a benefit of the asset in rate base from 2004 to 2006 and that North Bay did not file an application to recover the loss on the asset that was sold to a third party.

Board staff submits that the write-down of capital property of $540,755 in 2002 and the loss on disposal of assets of $144,597 in 2004 should not true-up to ratepayers. Board staff submits that North Bay should move the transactions to TAXREC3 in the 2002 and 2004 SIMPIL models respectively and that North Bay should re-file the corrected 2002 and 2004 SIMPIL models, PILs continuity schedule and EDDVAR continuity schedule.

Other than the adjustments for 2001 fourth quarter and 2002 PILs entitlement and the fixed asset transactions as discussed above, and any resulting changes to interest carrying charges, Board staff submits that North Bay has followed the regulatory guidance and the Board's decisions in determining the amounts recorded in Account 1562.

ACCOUNT 1521 – SPECIAL PURPOSE CHARGE ("SPC")

Background

On April 9, 2010, the Board issued a letter and invoice to all licensed electricity distributors outlining the amount of each distributor's SPC assessment and the associated SPC.

On April 23, 2010, the Board issued a letter to all licensed electricity distributors authorizing Account 1521, Special Purpose Charge Assessment Variance Account. Any difference between the amount remitted to the Ministry of Finance for the SPC assessment and the amount recovered from customers was to be recorded in "Sub-account 2010 SPC Assessment Variance" of Account 1521.

The letter also indicated, in accordance with section 8 of the SPC regulation, electricity distributors are required to apply to the Board no later than April 15, 2012 for an order authorizing them to clear any debit or credit balance in the "Sub-account 2010 SPC Variance". The Board expected that requests for disposition in "Sub-account 2010 SPC Variance" and "Sub-account 2010 SPC Assessment Carrying Charges" would be addressed as part of the proceedings for the 2012 rate year, except in cases where this approach would result in non-compliance with the timeline set out in section 8 of the SPC Regulation. In addition, the letter indicated in accordance with section 9 of the SPC Regulation, recovery of the SPC assessment is to be spread over a one-year period.

North Bay recovered the SPC from customers over a one year period beginning May 1, 2010. In response to Board staff interrogatory #3, North Bay completed the following table which indicates a residual balance of $6,177.50 for disposition, comprising principal as of December 31, 2011 and interest to April 30, 2012.

SPC Assessment (Principal Balance)	Amount recovered from customers in 2010	Carrying Charges for 2010	December 31, 2010 Year End Principal Balance	December 31, 2010 Year End Carrying Charges	Amount recovered from customers in 2011 (Jan.1 to Apr.30)	Carrying Charges for 2011	Forecasted December 31, 2011 Year End Principal Balance	Forecasted December 31, 2010 Year End Carrying Charges	Forecasted Carrying Charges for 2012 (Jan.1 to Apr.30)	Total for Disposition (Principal & Interest)
221,575.00	134,948.58	690.10	86,626.42	690.10	81,487.84	323.70	5,138.58	1,013.80	25.12	6,177.50

Submission

Board staff notes that the usual practice by the Board is to dispose of audited deferral and variance account balances. The balances in the table above provided by North Bay are not audited. Board staff notes that the residual balance in Account 1521 captures the difference between the assessed amount and the amounts recovered from ratepayers which arise as a result of the volume used in deriving the assessment unit rate (i.e. $0.0003725) and the actual volume consumed over the recovery period.

Board staff submits that despite the usual practice, the Board should authorize the disposition of Account 1521 as of December 31, 2010, plus the amount recovered from customers in 2011, including carrying charges as of April 30, 2012, because the account balance does not require a prudence review, and electricity distributors are required by regulation to apply for disposition of this account by April 30, 2012 in any event. It is Board staff's view that that there is no need to await the outcome of final audited results when these results may be available after April 30, 2012.

Consistent with the treatment of Group 1 account balances and account 1562, Board staff submits that a disposition period of two year should also be used.

Shared Tax Savings

Background

North Bay proposed that an amount of $15,638 related to the sharing of tax savings owed to customers be recorded in variance account 1595 consistent with the treatment approved by the Board in the 2011 IRM Decision.

Submission

Board staff notes that there are discrepancies between the regulatory taxable income used by North Bay in the 2012 Shared Tax Savings Workform and the regulatory taxable income included in the 2010 Revenue Requirement Work Form ($2,313,638 versus $1,649,160). This change would increase the amount to be returned to ratepayers from $15,638 to $102,200. Board staff invites North Bay to comment on this adjustment in its reply submission and indicate, given the magnitude of the refund, whether it still proposes to record this amount in account 1595 for future disposition.

LRAM CLAIM

Background

The Board's *Guidelines for Electricity Distributor Conservation and Demand Management* (the "CDM Guidelines") issued on March 28, 2008 outline the information that is required when filing an application for LRAM or SSM recovery.

North Bay originally sought to recover a total LRAM claim of $187,545 over a two-year period. The lost revenues include the effect of CDM programs delivered in 2008, 2009 and 2010 and the persisting energy savings between January 1, 2008 and April 30, 2012. North Bay used final 2010 OPA program results to calculate its LRAM amount. The LRAM amount was updated in response to interrogatories from Board staff and VECC to $97,210 due to North Bay having discovered it had not adjusted the LRAM claim by the projected CDM kWh savings from its approved 2010 load forecast.

The Board's *Guidelines for Electricity Distributor Conservation and Demand Management* (the "Guidelines") issued on March 28, 2008 outlines the information that is required when filing an application for LRAM. In its decision on Horizon's application (EB-2009-0192) for LRAM recovery, the Board also noted that distributors should use the most current input assumptions available at the time of the third party review when calculating a LRAM amount.

Submission

2010 programs and persisting impacts of 2008-2010 programs

North Bay has requested the recovery of an LRAM amount that includes the effect of new 2010 programs as well as persistence for 2008 and 2009 programs in 2010 and persistence of 2008-2010 programs from January 1, 2011 to April 30, 2012.

Board staff notes that North Bay's rates were last rebased in 2010.
Board staff notes that the CDM Guidelines state the following with respect to LRAM claims:

> Lost revenues are only accruable until new rates (based on a new revenue requirement and load forecast) are set by the Board, as the savings would be assumed to be incorporated in the load forecast at that time[3].

Board staff also notes that in its Decision and Order in the EB-2011-0174 proceeding, the Board disallowed LRAM claims for the rebasing year as well as persistence of prior

3 Section 5.2: Calculation of LRAM, Guidelines for Electricity Distributor Conservation and Demand Management (EB-2008-0037)

year programs in and beyond the test year on the basis that these savings should have been incorporated into the applicant's load forecast at the time of rebasing.

In cases in which it was clear in the application or settlement agreement that an adjustment for CDM was not being incorporated into the load forecast specifically because of an expectation that an LRAM application would address the issue, and if this approach was accepted by the Board, then Board staff would agree that an LRAM application is appropriate. North Bay may want to highlight in its reply whether the issue of an LRAM application was addressed in their cost of service application.

In the absence of the above information, Board staff therefore does not support the recovery of the requested persisting lost revenues from 2008 and 2009 CDM programs in 2010, the lost revenues from 2010 CDM programs, or the lost revenues from 2008-2010 CDM programs persisting from January 1, 2011 to April 30, 2012 as these amounts should have been built into North Bay's last approved load forecast.

2008 and 2009 programs

Board staff notes that North Bay has not collected 2008 lost revenues from OPA CDM programs and the lost revenues associated with both 2009 third tranche CDM programs and 2009 OPA CDM programs, years during which North Bay was under IRM. Board staff supports the approval of the 2008 and 2009 lost revenues requested by North Bay as these lost revenues took place during IRM years and North Bay did not have an opportunity to recover these amounts. Board staff notes that this is consistent with what the Board noted in its decisions on applications from Horizon (EB-2011-0172), Hydro One Brampton (EB-2011-0174), and Whitby Hydro (EB-2011-0206).

Board staff requests that North Bay provide an updated LRAM amount that only includes lost revenues from 2008 and 2009 CDM programs in the years 2008 and 2009 and the subsequent rate riders.

All of which is respectfully submitted