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Ontario

BY EMAIL

January 27, 2012

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: Waterloo North Hydro Inc.
2012 IRM3 Distribution Rate Application
Board Staff Submission
Board File No. EB-2011-0201

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

In addition please remind Waterloo North Hydro Inc. that its Reply Submission is due by February 6, 2012.

Yours truly,

Original Signed By

Georgette Vlahos
Analyst, Applications & Regulatory Audit

Encl.

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2012 ELECTRICITY DISTRIBUTION RATES

Waterloo North Hydro Inc.

EB-2011-0201

January 27, 2012

Board Staff Submission
Waterloo North Hydro Inc.
2012 IRM3 Rate Application
EB-2011-0201

Introduction

Waterloo North Hydro Inc. ("Waterloo North") filed an application (the "Application") with the Ontario Energy Board (the "Board") on October 26, 2011, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that Waterloo North charges for electricity distribution, to be effective May 1, 2012. The Application is based on the 2012 3rd Generation Incentive Regulation Mechanism ("IRM").

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 Waterloo North.

In the interrogatory phase, Board staff identified certain discrepancies in the data entered in the application model by Waterloo North. 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, Waterloo North confirmed that they were errors and provided the corrected data. Board staff will make the necessary corrections to Waterloo North's model at the time of the Board's Decision on the Application.

Waterloo North completed the Tax-Savings Workform with the correct rates and reflects the Revenue Requirement Work Form from the Board's cost of service decision in EB-2011-0144. Board staff has no concerns with the workform as filed.

Staff has no concerns with the data supporting the updated Retail Transmission Service Rates proposed by Waterloo North. Pursuant to Guideline G-2008-0001, updated on July 8, 2010, Board staff notes that the Board will update the applicable data at the time of this Decision based on any available updated Uniform Transmission Rates.

Waterloo North provided a reconciliation of Account 1521 – Special Purpose Charge as requested by Board staff during the interrogatory phase. Board staff notes that the usual practice by the Board is to dispose of audited deferral and variance account balances.

Board staff notes that the Board has approved the disposition of unaudited balances in account 1521 in both the Horizon (EB-2011-0172) and Hydro One Brampton (EB-2011-0174) 2012 IRM proceedings.

Based on Waterloo North's reconciliation, Board staff supports Waterloo North's request to dispose of the updated balance in this account of a credit of $20,464. Board staff submits that the Board should authorize the disposition of Account 1521 as of December 31, 2010, plus the amount recovered from customers in 2011, including the appropriate carrying charges. Board staff submits that if the Board decides to dispose of account 1521, the disposition should be on a final basis and account 1521 should be closed.

With respect to disposition period, Board staff submits that Account 1521 should be disposed of over a period of two years, along with Waterloo North's Group 1 Accounts, for the reasons set out below.

Board staff makes detailed submissions on the following matters:

- Review and Disposition of Deferral and Variance Accounts as per the *Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report");
- Smart Meter Funding Adder ("SMFA");
- Lost Revenue Adjustment Mechanism Claim; and
- Payments in Lieu of Taxes – PILS 1562.

REVIEW AND DISPOSITION OF DEFERRAL AND VARIANCE ACCOUNTS

Background

For the purpose of 2012 IRM applications, the EDDVAR Report requires a distributor to determine the value of its December 31, 2010 Group 1 Deferral and Variance account balances and determine whether the total balance exceeds the preset disposition threshold of $0.001 per kWh using the 2010 annual kWh consumption reported to the Board. When the preset disposition threshold is exceeded, a distributor is required to file a proposal for the disposition of Group 1 account balances (including carrying charges) and include the associated rate riders in its 2012 IRM Rate Generator for the disposition of the balances in these accounts. The onus is on the distributor to justify why any account balance should not be cleared if the threshold is exceeded.

Submission

Waterloo North completed the Deferral and Variance Account continuity schedule included in the 2012 IRM Rate Generator Model at Tab 9 for its Group 1 Deferral and Variance Accounts. Waterloo North's total Group 1 Deferral and Variance Account balances amount to a credit of $2,996,702 which includes interest calculated to April 30, 2012. Based on the threshold test calculation, the Group 1 Deferral and Variance Account balances equate to $0.00215 per kWh which does exceed the threshold, and as such, Waterloo North requested disposition of these Accounts over a four year period.

Board staff has reviewed Waterloo North's Group 1 Deferral and Variance account balances and notes that the principal balances as of December 31, 2010 reconcile with the balances reported as part of the *Reporting and Record-keeping Requirements*. Also, the preset disposition threshold has been exceeded. Accordingly, Board staff has no issue with Waterloo North's request to dispose of its 2010 Deferral and Variance Account balances at this time.

Board staff does however takes issue with the disposition period (i.e. four years) requested by Waterloo North. Board staff notes that Waterloo North's Application is not consistent with the guidelines outlined in the EDDVAR Report with respect to the standard disposition period for Group 1 accounts (i.e. one year). In its interrogatory responses, Waterloo North provided rate riders and bill impacts for one and two year disposition periods in the repayment of all Group 1 Accounts as requested by Board staff.

			4 Year		1 Year				2 Year			
			WNH Application		IR # 6							
Rate Class	Monthly Consumption		$ (Decrease) on Total Bill	% (Decrease) on Total Bill	$ (Decrease) on Total Bill	% (Decrease) on Total Bill	$ Change vs 4 Years	% Change vs 4 Years	$ (Decrease) on Total Bill	% (Decrease) on Total Bill	$ Change vs 4 Years	% Change vs 4 Years
	kWh	kW										
Residential	800		(1.17)	-1.08%	(3.45)	-3.19%	(2.28)	-2.11%	(1.99)	-1.84%	(0.82)	-0.76%
GS < 50 kW	2,000		(2.30)	-0.89%	(6.97)	-2.69%	(4.67)	-1.80%	(3.72)	-1.43%	(1.42)	-0.55%
GS > 50 kW	100,000	250	(71.81)	-0.69%	(280.84)	-2.69%	(209.03)	-2.00%	(141.51)	-1.35%	(69.70)	-0.67%
Large User	7,000,000	12,300	(3,815.93)	-0.58%	(14,995.30)	-2.27%	(11,179.38)	-1.69%	(7,542.39)	-1.14%	(3,726.46)	-0.56%
USL	250		(0.71)	-1.58%	(1.76)	-3.90%	(1.04)	-2.32%	(1.06)	-2.36%	(0.35)	-0.78%
Street Light	50	0.14	(0.07)	-1.14%	(0.20)	-3.13%	(0.13)	-1.99%	(0.11)	-1.70%	(0.04)	-0.57%
Embedded Distributor	2,375,000	6,000	(1,216.13)	-0.64%	(4,844.99)	-2.54%	(3,628.85)	-1.90%	(2,425.55)	-1.27%	(1,209.41)	-0.63%

The table above provided by Waterloo North summarizes the dollar and percentage impacts of each of the three disposition periods. All of the rate riders proposed by Waterloo North in its Application are included in the calculations above, namely Group 1 Accounts, PILs 1562, SPC and LRAM[1].

Waterloo North requested a four-year disposition period citing that refunding the credit balance of $2,996,702 over a shorter time frame (i.e. one or two years) would result in customers experiencing a larger rate increase when the rate riders cease[2]. Waterloo North also noted that it has the majority of its 2010 and 2011 rate riders ceasing in 2014. To cease the 2012 rate riders in 2013 or 2014 would have Waterloo North's customers experience either two years in a row of increased rates due to cessation of rate riders (2013 and 2014) or to experience an even larger rate increase in 2014 if a two year disposition was ordered[3].

Board staff notes that the balances in the subject accounts represent over recoveries on the part of the distributor and in the normal course should be available to be refunded over a fairly short time frame.

While recognizing the value of the EDDVAR Report in guiding decisions with respect to the disposition of deferral and variance accounts, 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 Accounts over a four-year period. In that proceeding, Board staff submitted that while some volatility in customer bills may occur, it is 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 may be 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 the current application, regarding Group 1 account balances, Board staff notes that using a disposition period as long as four years would exacerbate intergenerational inequities. Board staff however recognizes that some volatility in electricity bills may result from adopting a shorter disposition period, as seen in the table above. Board staff

[1] EB-2011-0201, Interrogatory Responses, Page 19
[2] EB-2011-0201, Interrogatory Responses, Page 2
[3] *Ibid*

is of the view that the Board should strike a balance between reducing intergenerational inequities and mitigating rate volatility.

Staff recommends that a two-year disposition period should be adopted for all Group 1 accounts.

SMART METER FUNDING ADDER ("SMFA")

Background

In its original application, Waterloo North proposed to maintain the $1.00 SMFA for the 2012 rate year. Waterloo North provided a table which demonstrated that only 84.7% of the total anticipated Smart Meter Costs have been audited as opposed to the 90% which the Board expects for which the distributor is seeking to recover. Waterloo North also documents that as at December 31, 2011 it estimated 100% meter deployment. Waterloo North noted that it has also received approval for a TOU extension to January 31, 2012 for certain customers and the costs to apply TOU pricing for these customers is uncertain[4].

In a response to a Board staff interrogatory, Waterloo North noted that the current SMFA of $1.00 would only provide partial recovery of the revenue requirement for installed smart meters The Smart Meter Model in IR#8 (B)(ii) calculated a SMFA of $1.37. As such, Waterloo North is seeking to increase its SMFA in this application to $1.37 in order to avoid a significant deferred revenue requirement recovery and rate impact when Waterloo North makes an application for disposition.

Submission

Waterloo North states that due to it's TOU extension, it has remaining costs to incur, as seen in the table below, totalling approximately $537,000.

Section	Details	2011	2012
2.1.1	Maintenance (may include meter reverification costs, etc.)		92,101
2.3.2	Usage Fees to Smart Meter Provider to obtain meter reads	13,938	191,100
2.5.6	Meter Base Repair/Relocation Material & Parts	6,869	
	Tower - Electricity Usage	1,267	
2.6.3	Compensation & Expenses **	124,156	100,000
Total		**146,230**	**383,201**

[4] EB-2011-0201, Application, Page 40

Board staff also notes that Waterloo North does not have 90% of total smart meter costs audited, to support its proposal for a final prudence review.

However, Board staff notes that Waterloo North has completed 100% of its smart meter deployment. The SMFA was a tool designed to provide advanced funding and to mitigate the anticipated rate impact of smart meter costs when recovery of those costs is approved by the Board (G-2008-0002). It was not intended to be compensatory on a cumulative basis over the term the SMFA was in effect. On that basis, Board staff would generally not support the continuation of the SMFA. However, Board staff considers that cessation of the SMFA without replacement by an SMDR or SMIRR until a utility's application for smart meter cost disposition can be concluded several months later would create rate fluctuations, and possibly result in customer confusion. Further, the total deferred revenue requirement would continue to increase in the absence of even partial recovery through an SMFA. Board staff therefore submits that the Board may wish to consider continuation of the originally requested $1.00 SMFA until it is replaced by an SMDR and SMIRR resulting from the Board's decision in a smart meter cost disposition application. The Board has not yet assessed the smart meter costs for prudence and therefore the approval of the $1.00 SMFA rather than $1.37 would reduce the risk of over recovery should some of the costs be disallowed.

With this in mind, Board staff submits that the Board may wish to consider continuance of the SMFA with a specific termination date. Board staff notes that Waterloo North has requested that the SMFA be extended to April 30, 2013. If Waterloo North was expected to rebase its rates through a Cost of Service application for that year, then that extension might be reasonable. However, Waterloo North last rebased its rates for 2011, and its next rebasing is scheduled for 2015.

Board staff is of the view that establishing a termination date of October 31, 2012 for the SMFA would be reasonable. By that time, Waterloo North should have completed its smart meter program, including TOU implementation. The 2011 costs would also be audited, so that total smart meter costs should satisfy the threshold that at least 90% of such costs are audited actuals. Further, this will allow sufficient time for the utility to prepare and file an application in accordance with the recently issued SMF Guideline and model and for the Board to process such an application. Board staff notes that such an application should be filed by no later than May 31, 2012 to allow sufficient time for the application to be processed in time for a October 31, 2012 implementation.

Board staff observes that this treatment has also been proposed by other utilities. Board staff submits that this approach should be practical in terms of the workload on utility staff and the Board, and also be reasonable with respect to the impacts on rates for customers, while facilitating the timely and practical recovery of the deferred revenue requirement for installing smart meters and associated equipment and operations.

LOST REVENUE ADJUSTMENT MECHANISM ("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.

Waterloo North originally sought to recover a total LRAM claim of $161,037, including carrying charges, over a four-year period. Waterloo North is requesting recovery of 2010 LRAM amounts, which include persisting lost revenues in 2010 from CDM programs implemented from 2006-2009 and new 2010 lost revenues from 2010 CDM programs. Waterloo North's original claim used preliminary 2010 OPA program results as a best estimate in advance of receiving final 2010 results. Waterloo North subsequently updated its LRAM claim to $161,309, including carrying charges, based on the OPA's 2010 final program results.

The Board's CDM Guidelines 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 LRAM amount

Board staff notes that Waterloo North had its last load forecast approved by the Board as part of its 2011 Cost of Service application. Board staff supports the approval of LRAM amount requested by Waterloo North as these lost revenues took place during an IRM year and Waterloo North did not previously recover these amounts. Board staff notes that this is consistent with what the Board noted in its 2012 IRM decisions on applications from Horizon (EB-2011-0172), Hydro One Brampton (EB-2011-0174), and Whitby Hydro (EB-2011-0206). In addition, Board staff submits that, consistent with its submission on the disposition period for Group 1 Accounts, the Board might consider approving a disposition period of two years.

PAYMENTS IN LIEU OF TAXES – PILS 1562

Background

The PILs evidence filed by Waterloo North in this proceeding includes tax returns, financial statements, Excel models from prior applications, calculations of amounts recovered from customers, SIMPIL[5] Excel worksheets and continuity schedules that show the principal and interest amounts in the account 1562 deferred PILs balance. In pre-filed evidence Waterloo North applied to refund to customers a credit balance of $1,251,284 consisting of a principal amount of $1,222,774 plus related carrying charges of $28,510.

Submission

<u>Excess Interest True-up Calculations</u>
When the actual interest expense, as reflected in the financial statements and tax returns, exceeds the maximum deemed interest amount approved by the Board, the excess amount is subject to a claw-back penalty and is shown in sheet TAXCALC as an extra deduction in the true-up calculations.

Waterloo North replied to Board staff's interrogatories and provided a table that discloses the components of its interest expense for the period 2001 to 2005.[6]

[5] Spreadsheet implementation model for payments-in-lieu of taxes
[6] Response to Board Staff Interrogatories dated January 12, 2012/pg58.

	Oct - Dec 2001	2002	2003	2004	2005
Interest Expense per Financial Statement	**262,882**	**1,393,332**	**4,224,700**	**3,326,755**	**3,113,954**
Breakdown:					
Senior long-term notes payable	272,728	1,250,000	2,995,533	1,828,282	1,525,699
Junior long-term notes payable		-	1,360,681	1,360,681	1,359,145
Other debt:					
Interest on Holding Company Loan	21,725	176,626	103,890		
Customer Deposit Interest		5,343	12,019	21,584	42,888
Remittance/Arrears - HST/OEFC			2,026	21,904	
Bank Loan Interest				354,111	512,602
Other Interest Expense	1,078		205	9	
Interest Income	(32,649)	(38,637)	(249,655)	(259,816)	(326,381)
Total	**262,882**	**1,393,332**	**4,224,700**	**3,326,755**	**3,113,954**

Waterloo North reduced interest expense by deducting interest income in each year. The Board decided in EB-2011-0174 that Hydro One Brampton's interest expense used to calculate the interest claw-back variance should not include a deduction of interest income.[7]

As disclosed in the table above, Waterloo North has also included customer deposit interest and remittance/arrears - HST/OEFC. The Board decided in EB-2011-0174 that Hydro One Brampton's interest expense used to calculate the interest claw-back variance should not include interest on customer deposits. The remittance/arrears - HST/OEFC have not been highlighted in other cases to the best knowledge of Board staff, and Board staff is not certain that this penalty should be included in the SIMPIL claw-back variance calculations.

Waterloo North should clarify if the remittance/arrears - HST/OEFC are in fact penalties or interest assessed for late payments. If Waterloo North confirms that remittance/arrears - HST/OEFC are related to interest, Board staff submits that these interest amounts should be included in the interest claw-back variance calculations.

Board staff submits that interest on customer deposits should be deducted from total interest expense per the financial statements to be consistent with the decision for Hydro One Brampton.

[7] EB-2011-0174, December 22, 2011, pg9-10

Board staff submits that to be consistent with the decision for Hydro One Brampton, interest income should not be deducted in determining the interest expense to be used in the interest claw-back variance calculations.

Waterloo North should change the amount of interest expense used in the 2001-2005 SIMPIL model interest claw-back penalty calculations to reflect Board staff's submissions, and update the PILs 1562 continuity schedule and balance to be refunded to customers. Waterloo North should file a schedule of revised interest expense identifying the components in a format similar to that above shown.