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BY EMAIL

March 7, 2012

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, Suite 2700
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: Guelph Hydro Electric Systems Inc. Application for 2012 Rates
Board File No.: EB-2011- 0123

In accordance with the Board's decision dated February 22, 2012, attached are Board staff's comments on Guelph Hydro Electric Systems Inc.'s draft rate order, filed on February 29, 2012. Please forward the attached to Guelph Hydro Electric Systems Inc. and to all other registered parties to this proceeding.

Yours truly,

Original signed by

Birgit Armstrong
Advisor, Applications and Regulatory Audit

Attachment

ONTARIO ENERGY BOARD

2012 ELECTRICITY DISTRIBUTION RATES

Guelph Hydro Electric Systems Inc.

EB-2011-0123

STAFF SUBMISSION

DRAFT RATE ORDER

March 7, 2012

INTRODUCTION

Guelph Hydro Electric Systems Inc. ("Guelph Hydro" or the "Applicant") filed a Cost of Service application (the "Application") with the Ontario Energy Board (the "Board") on June 30, 2011. The Application was filed under section 78 of the *Ontario Energy Board Act, 1998* (the "Act"), seeking approval for changes to the rates that Guelph Hydro charges for electricity distribution to be effective January 1, 2012. The Board assigned the Application file number EB-2011-0123.

On February 22, 2012, the Board issued its Decision and Order on Guelph Hydro's application for 2012 electricity rates. The Decision required Guelph Hydro to file its draft rate order ("DRO") within seven business days of the issuance of the Decision. Guelph Hydro filed its DRO and supporting documentation on February 29, 2012. The following are Board staff's comments regarding the DRO.

Smart Meter Disposition Rate Rider

In the Board's decision, the Board found that the Zigbee chip included in the smart meters purchased and installed by Guelph were not related to smart meter deployment, and the costs (about $12.25/meter for a total capital amount of $600,000) should be removed from Account 1555.

In its draft rate order ("DRO") filing, Guelph Hydro filed an updated smart meter model spreadsheet and a spreadsheet to calculate class-specific smart meter disposition riders ("SMDRs") in accordance with the Board's Decision.

Board staff has reviewed Guelph's DRO filing and both spreadsheets, and offers submissions on Guelph's smart meter cost recovery proposal in the following areas:

- Removal of capital costs for the Zigbee chip;
- Impact of continued Smart Meter Funding Adder ("SMFA") revenues after December 31, 2011;
- Allocation of SMFA revenues to calculate class-specific SMDRs;

Board staff has attached a revised version of the Smart Meter Model and a class-specific SMDR spreadsheet to address the above issues.

Removal of capital costs for the Zigbee chip

Board staff submits that Guelph Hydro has appropriately removed the capital costs for the Zigbee chip, estimated at $600,654, from row 103 on sheet “2. Smart_Meter_Costs” of the smart meter model.

Impact of continued SMFA revenues after December 31, 2011

In its application, Guelph Hydro proposed an effective date for rates of January 1, to align the rate year with the (calendar) fiscal year. In its smart meter model it assumed acceptance of this proposal. In particular, in the smart meter model, on sheet “8. Funding_Adder_Revs”, Guelph included estimated SMFA revenues and calculated interest to the end of December 2011. If Guelph Hydro’s new rates had been effective <u>and</u> implemented January 1, 2012, as proposed, this would be appropriate. However, Guelph Hydro’s current Board-approved rates, from its 2011 IRM application continue to apply until March 31, 2012. The Board approved a SMFA of $1.17/month to be collected from each metered customer until April 30, 2012. Thus, Guelph Hydro continues to collect the SMFA into 2012, at a level of about $60K per month.

Board staff submits that since Guelph Hydro’s new rates will be implemented April 1, 2012, it would be appropriate to calculate the additional SMFA and interest on principal for 2012 Q1. Board staff submits that the Board, in its Rate Order, could cease the SMFA as of March 31, 2012. In the Smart Meter Model spreadsheet attached to this submission, Board staff has revised sheet 8 to reflect the additional SMFA revenues and interest to March 31, 2012. With final disposition of smart meter costs, the SMFA is no longer needed, and is replaced by the SMDR which recovers or refunds the deferred incremental revenue requirement net of SMFA revenues and interest. There should be no overlap.

Allocation of SMFA to calculate class-specific SMDRs

Guelph Hydro has included a separate spreadsheet to calculate class-specific SMDRs for the Residential and GS < 50 kW classes. Board staff’s review of the methodology suggests that the approach for allocating the capital and operating costs is reasonable. Guelph Hydro allocated the revenue generated from the Smart Meter Funding Adder to the customer classes based on the percentage of costs allocated to customer classes.

Board staff takes issue with this methodology. This approach results in an unintuitive situation where the credit SMDR for the GS < 50 kW, of ($0.96)/month for 12 months, would be larger than the credit SMDR for the Residential class of ($0.29)/month for twelve months.

Guelph's spreadsheet allocates 78.97% of the SMFA revenues and interest to the Residential class and 21.03% to the GS < 50 kW class. However, based on Guelph Hydro's customer counts in its load forecast, and looking over the historical data from May 2006 to December 2011, Residential customers represent 91.42% of Guelph Hydro's metered customers. With a uniform or "postage stamp" SMFA in effect at any point in time, it means that Residential customers contributed that percentage of SMFA revenues.

Board staff submits that the methodology for allocating SMFA revenues and associated interest should be as follows:

- SMFA revenues for the Residential and GS< 50 kW classes should be directly allocated. A simple way of doing this is to multiply the SMFA revenues and interest by the percentage of metered customers that each of these classes represents from the period from May 2006 to December 2011 (or March or April 2012, if appropriate);
- For the remaining SMFA revenues collected from other classes (i.e. GS > 50 kW), these residual SMFA revenues and interest are allocated between the Residential and GS < 50 kW customer classes evenly as determined by the Board in a recent Decision and Order (EB-2011-0128).

Board staff has prepared an alternative cost allocation spreadsheet to implement this approach. Under this approach, 92.36% of SMFA revenues and interest would be allocated to the Residential class, and 7.64% of SMFA revenues and interest would be allocated to the GS < 50 kW class. Using this approach, and taking into account the SMFA revenues and interest to March 31, 2012, Board staff submits that a Residential SMDR of ($1.15)/month for 12 months, and a GS < 50 kW SMDR of $5.85/month for 12 months, would be appropriate. While the quanta of these class-specific SMDRs are surprising, the relationship is logical; GS < 50 kW customers with more expensive meters on average do not get a higher credit (and in fact owe more in terms of the deferred revenue requirement) compared to Residential customers.

Board staff acknowledges that the methodology issue could have been addressed during the hearing. However, it is mainly with the increased amounts that have arisen as a result of the Board's decision (the removal of Zigbee chip costs and three additional months of SMFA revenues) that the impact of the incorrect cost allocation has been exacerbated.

IFRS-CGAAP Transitional PP&E Amounts

In the DRO Guelph Hydro presented the treatment of the PP&E Deferral account as a result of the transition from CGAAP to MIFRS in accordance with the Settlement Agreement. Guelph Hydro calculated a credit balance of $1,526,000 in the PP&E deferral account to be refunded to rate payers. Guelph Hydro proposed an amortization period of four year. The resulting downward adjustment to revenue requirement is $485,000 ($382,000 Depreciation expense + $104,000 Return on Rate base at WACC – 2012 6.80%). Board staff has no issue with the calculation of the credit balance.

However, Guelph Hydro noted that it adjusted/lowered the 2012 revenue requirement by $1,526,000 (difference in closing net PP&E (CGAAP versus MIFRS)) and by $485,000 (amortization and return on rate base). On page 11 Guelph Hydro stated that the 2012 Rate Base has been adjusted accordingly to $139,104,469. In support, Guelph Hydro showed a Fixed Asset Continuity Schedule as of December 31, 2012, which shows the addition of a $1,526,000 credit amount to adjust gross fixed assets for the 2012 test year. Guelph Hydro also included a credit amount of $381,500 as an addition to accumulated deprecation.

In the Addendum to Report of the Board: Implementation International Financial Reporting Standards in an Incentive Rate Mechanism Environment (EB-2008-0408), with respect to the disposition of PP&E deferral account balance, the Board determined the following:

> *The amortization of the adjusting amount [for the PP&E deferral account balance], up or down, will be reflected as an adjustment to depreciation expense (the refund or recovery of the amount of the adjustment over time) and the return on rate base calculation on the unamortized balance will be recovered in rates in the same way as for any other component of rate base.*

The downward adjustment relating to the PP&E deferral account to Guelph Hydro's 2012 revenue requirement has two components:

(1) A downward adjusting amount of $382,000 for the amortization of to the 2012 depreciation expense.
(2) A credit amount of $104,000 for the return on rate base as refund to the customers.

In the case of Guelph Hydro, which has recorded $1,526,000 in the PP&E deferral account, the downward adjustment should be $485,000 ($382,000 + $104,000) to the 2012 revenue requirement and continue in the three subsequent years (2013-2015) for which Guelph Hydro is under an Incentive Rate Mechanism regime. A downward adjustment of the depreciation expense of $382,000 should be made to the total depreciation expenses as a part of Guelph Hydro’s 2012 OM&A expenses. The credit amount of $104,000 for the calculated return on the rate base (which should not be recorded in PP&E deferral account) should be shown as a separate reduction line item to the 2012 revenue requirement as a refund to the customers when calculating the 2012 revenue requirement.

For accounting purposes, the amortization of the $1,526,000 credit balance recorded in the PP&E deferral account should consist of an offsetting entry of $382,000 to this account as an adjustment to depreciation expense in the 2012 test year and in the three subsequent years (2013-2015) for which Guelph Hydro is under an inventive Rate Mechanism regime.

It appears that Guelph Hydro’s 2012 Fixed Asset Continuity Schedule were prepared on MIFRS basis given that its transition year for the adoption of IFRS was 2010 and the year of adoption was 2011. However, the 2012 Fixed Asset Continuity Schedule was adjusted to include the PP&E deferral account balance of $1,526,000. This appears to have created a double counting situation. The Fixed Asset Continuity Schedule should not be adjusted for amounts recorded in the PP&E deferral account.

GEA Renewable Connection – Funding Adder Calculation

In Appendix G –GEA Renewable Connection – Funding Rate Adder Calculation, Guelph Hydro provided a calculation allowing for the inclusion of one Smart Grid Technician ($87,000/year) as well as capital cost for its renewable generation projects as per the Board’s Decision. Guelph Hydro noted that for the 2012 rate year the 2012 OM&A cost have been prorated for the remaining 9 month from April to December

($87,000X9/12=$65,250). Board staff takes no issue with this approach. However, Board staff noted that for the 2012 rate year, Guelph Hydro applied Cost of Capital parameters of ROE 9.58%, Deemed LT Debt rate of 5.26% and Deemed ST Debt rate of 2.46%. In a letter of November 10, 2011 the Board determined the following Cost of Capital parameters for rates effective January 1, 2012 ROE 9.42%; Deemed LT Debt rate 5.01% and Deemed ST Debt rate 2.08%. Board staff submits that Cost of Capital parameters effective January 1, 2012 should be used for the calculation of the 2012 GEA Renewable Connection Rate Adder.

On page 3 of Appendix G, Guelph Hydro provided a the following Direct Benefit calculation.

Average Net Fixed Assets	Direct Benefit %	2012	2013	2014	2015
Renewable Connections Capital - Expansions	17%	$ -	$ -	$ -	$ -
Renewable Connections Capital - Renewable Enabling Improvements	6%	$ -	$ 245,000	$ 504,500	$ 532,500
Feeder Automation Projects	100%	$ -	$ -	$ -	$ -
OM&A	6%	$ 65,250	$ 82,650	$ 91,350	$ 104,400
		$ 65,250	$ 327,650	$ 595,850	$ 636,900
Direct Benefit		$ 3,915	$ 19,659	$ 35,751	$ 38,214
Weighted Average Direct Benefit %		6.00%	6.00%	6.00%	6.00%

Board staff noted that the OM&A of $82,650 for 2013, $91,350 for 2014 and $104,400 for the 2015 rate year is not compliant with the Board's decision and seem to reflect an earlier GEA Funding Adder calculation. On page 2 of Appendix G, Guelph Hydro shows OM&A costs of $87,000 from 2013 through 2015 consistently. Board staff notes that in the *Report of the Board: Framework for Determining the Direct Benefits Accruing to Customers of a Distributor under Ontario Regulation 330/09* the Board determined that ongoing OM&A costs that are incurred by the distributor after the investment has been made will not be eligible for provincial recovery. Board staff submits that the Direct Benefit calculation has been applied correctly on page 2 of Appendix G. Board staff invites Guelph Hydro to comment on the calculation shown above and update if necessary.

IMPLEMENTATION

Guelph Hydro provided calculation of a forgone revenue rate rider to reflect the Board Decision of an effective date of January 1, 2012 and an implementation date of April 1, 2012 in Appendix I of the DRO. Board staff has reviewed these calculations and submits that Guelph Hydro has correctly calculated the foregone revenue rate rider to reflect a 9 month recovery period. Board staff has no issue with the calculation. However, Board staff has noted that the last column of the formula shows the formula as G=F/A/10. Board staff submits that this formula should read G=F/A/9.

On page 5 of the DRO Guelph Hydro proposed a sunset date of March 31 of the corresponding year for all new 2012 rate riders and adders listed in the tariff of Rates and Charges, including those not mentioned specifically in the Board's Decision. Board staff takes no issues with this approach.

- All of which is respectfully submitted -