PUBLIC INTEREST ADVOCACY CENTRE
LE CENTRE POUR LA DEFENSE DE L'INTERET PUBLIC
ONE Nicholas Street, Suite 1204, Ottawa, Ontario, Canada K1N 7B7
Tel: (613) 562-4002. Fax: (613) 562-0007. e-mail: piac@piac.ca. http://www.piac.ca

Michael Buonaguro
Counsel for VECC
(416) 767-1666

March 30, 2008

VIA MAIL and E-MAIL

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

Dear Ms. Walli:

Re: Vulnerable Energy Consumers Coalition (VECC)
Final Submissions: EB-2007-0931
PUC Distribution Inc. – 2008 Electricity Distribution Rate Application

Please find enclosed the final submissions of the Vulnerable Energy Consumers Coalition (VECC) in the above-noted proceeding. We have also directed a copy of the same to the Applicant.

Yours truly,

Michael Buonaguro
Counsel for VECC
Encl.

EB-2007-0931

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sch. B, as amended;

AND IN THE MATTER OF an Application by PUC Distribution Inc. pursuant to section 78 of the *Ontario Energy Board Act* for an Order or Orders approving just and reasonable rates for the delivery and distribution of electricity.

FINAL SUBMISSIONS

On Behalf of The

VULNERABLE ENERGY CONSUMERS COALITION (VECC)

March 29, 2008

Michael Buonaguro
Public Interest Advocacy Centre
34 King Street East
Suite 1102
Toronto, Ontario
M5C 2X8

Tel: 416-767-1666
E-mail: mbuonaguro@piac.ca

Vulnerable Energy Consumers Coalition (VECC)
Final Argument

1 The Application

1.1 On November 30, 2007 PUC Distribution Inc. ("PUC") submitted an Application to the Ontario Energy Board for approval of its proposed 2008 distribution rates. This application is based on a projected 2008 Distribution revenue requirement[1] of $17,191,211 which, after an allowance of $972,721 for revenue from other sources, leaves $16,218,490 to be recovered through distribution rates. Excluded from this amount is the "cost" of the transformer ownership allowance[2] ($86,864).

1.2 Distribution revenues for 2008 at current rates (including the smart meter and prior to the transformer allowance) would produce base revenues of $12,105,168[3] yielding a difference of $4,200,186[4] or 34.7%.

1.3 Also included in the Application is a request to clear the balances in a number of deferral and variance accounts.

1.4 The following sections contain VECC's final submissions regarding the various aspects of PUC's Application.

[1] Exhibit 9, page 2
[2] VECC #14 a)
[3] VECC #4 c)
[4] $16,218,490+$86,864-$12,105,168=$4,200,186

2 <u>Rate Base and Capital Spending</u>

Capital Spending

2.1 PUC's capital spending for 2007 and 2008 is driven primarily by[5]:

- Customer Demand Projects (New/Upgraded Services),
- Renewal Projects,
- Voltage Conversions, and
- Smart Meters.

2.2 VECC has no submissions regarding the spending on Customer Demand Projects. VECC is concerned that PUC is not currently carrying out the required economic evaluations for such projects in order to establish whether or not capital contributions are required[6]. PUC has indicated that it intends to review its handling of capital contributions. However, to the extent there is no allowance included in the rate base for such contributions, rates for 2008 will be overstated if any contributions are subsequently established during this year. In order to address this issue VECC submits that the OEB should approve spending levels for Customer Demand Projects (for purposes of rate base determination) that are nominally (e.g., 10%) less than requested.

2.3 PUC has filed both internally prepared[7] as well as 3rd party reports[8] documenting the condition of its system and the need to both complete its voltage conversion project initiated in the 1960's and renew its existing infrastructure. VECC has no submissions regarding the need for the proposed work.

2.4 VECC is concerned about whether PUC will be able to obtain and deploy the resources needed to complete the proposed 2008 system renewal and voltage conversion projects. PUC was unable to meet its budgeted 2007 capital

---

[5] Exhibit 2, Tab 3, Schedule 3, page 2 and page 12
[6] OEB Staff #23 d)
[7] Exhibit 2, page 42
[8] Exhibit 2, pages 85 and 127

spending[9] due to both internal staffing issues and the lack of contractor resources. Forecast spending levels for 2008 are even higher[10]. VECC requests that PUC address this issue in its reply submissions. Failing a satisfactory response based on the evidence filed, the OEB should consider reducing the 2008 spending levels closer to 2007 values.

2.5 Over half of PUC's 2008 capital spending is related to Smart Meters[11]. VECC's views on the 2008 treatment of PUC's Smart Meter related costs are set out in the Smart Meter section of this submission. However, in summary, it is VECC's position that Smart Meter capital should not be included in PUC's rate base but rather the impact recorded in Variance/Deferral Account #1555.

2.6 Finally, while not specifically referenced in Exhibit 2, the response VECC #18 a) suggests that the Cost Allocation Study leads to an increased allocation of PUC Distribution cost to capital of $738,344(i.e., the change in allocation to Fixed Assets). VECC requests that PUC confirm this interpretation of the response in its reply submissions.

Rate Base

2.7 Rate Base consists of Net Fixed Assets plus an allowance for working capital. In determining working capital PUC has used 15% of OM&A plus Cost of Power and has used $55 / MWh to determine the commodity portion of Cost of Power[12]. No explanation was provided as to the source of this value. However, VECC notes it is reasonably close to the most recent forecast available from Navigant of over $54 / MWh[13].

2.8 PUC has also not provided any details regarding the basis for the Transmission Network Charges used in determining its working capital requirements. However,

---

[9] Board Staff #23 a)
[10] Exhibit 2, pages 30-32
[11] Exhibit 2, page 33
[12] VECC #6 ($41,062,669/746,593.973)
[13] www.oeb.gov.on.ca/documents/cases/EB-2004-0205/rpp-nci_wholesaleelectricitypriceforecastreport_20071012.pdf - page 2. Where HOEP for 2008 is projected to be in the order of $0.054 / kWh.

with volumes increasing by 11.5% and cost declining by 3.7%[14], it appears that PUC has assumed a price change for Network Services of roughly 15%. VECC notes that this is less than the decrease in Transmission Network charges that was recently approved by the OEB. Unless PUC can explain the discrepancy VECC submit that the Transmission Network charges should be reduced so as to align with the new wholesale network transmission rates.

3 Load Forecast and Revenue Offsets

Load Forecast

3.1 PUC has used 2004 weather normalized load data developed by Hydro One Networks to establish a weather-normalized average customer use for each weather-sensitive customer class. It has then developed its load forecast by multiplying this average (per customer) use for each customer class by the forecast 2008 customer count (by class)[15]. For unmetered loads (Street Lighting, Sentinel Lighting and USL), average use per connection from 2003-2006 was applied to the forecasted number of 2008 connections[16]. VECC has no submissions with respect to PUC's load forecast.

3.2 Board Staff has expressed concerns regarding the fact that PUC's approach relies on a single year of weather-normalized historical data to determine future load[17]. VECC has similar concerns, which it has already expressed in submissions made regarding other electricity distributors' 2008 rates. However, in the short-term it is not clear to VECC that a better alternative exists.

3.3 In response to a Board Staff Information Request[18], PUC has attempted to produce weather-normalized usage values by customer class for 2002 through 2006 using IESO province-wide weather correction factors. In its submissions

[14] VECC #6 a)
[15] OEB Staff #32 a)
[16] OEB Staff #32 b)
[17] OEB Staff Submissions, pages 20-21
[18] OEB Staff #35

Board Staff suggests that a load forecast based on this data would be more accurate[19] and seeks other party's comments.

3.4 VECC disagrees with the Board Staff's view that this alternate approach will yield a more accurate load forecast. The IESO weather factor used in the alternative analysis is a simple annual value based on the province overall. It does not reflect PUC's customer class mix, penetration rates for weather sensitive loads by class or the fact weather impacts vary across the province. While the Hydro One normalization process was based on 2004 data, its does account for all these factors. As a result, VECC believes PUC's original approach is preferable to the one presented in response to Staff #35.

Other Revenues

3.5 VECC has no submissions with respect to PUC's Other Revenues forecast.

4 <u>Operating Costs</u>

OM&A – General

4.1 In response to Board Staff information Request #4 PUC has provided an explanation of the $1,821,725 change in OM&A costs (excluding all taxes) from 2006 to 2008. Staff Submissions have identified the OM&A expense areas accounting for the majority of the cost increase[20]. The major cost drivers identified are labour rate increases, staff/external increases to meet system needs, a pension adjustment and smart meters.

4.2 The employee and compensation data provided by PUC was somewhat inconsistent in that the employee count included only the PUC Services staff whose "primary" function is to provide services to PUC Distribution, while the compensation data covered all employees. However, in response to information requests, PUC has reconciled the two and the implicit wage increases of 3%

[19] OEB Staff Submissions, page 21

appear reasonable[21].

4.3 PUC is forecasting material staff increases over the 2006-2008 period. However, these staff increases are generally supported by PUC's long term capital needs and OM&A study[22]. Having said this, VECC notes that the number of numerical inconsistencies identified by Board Staff[23] in the explanations provided and agrees that these need to be reconciled before the requested dollar values can be accepted.

4.4 With respect to the Pension Adjustment, PUC has not fully explained the nature of adjustment and why the 2007 adjustment of $350,000 is an ongoing cost for 2008. VECC submits that further information is needed before this cost item can be included in the 2008 revenue requirement.

4.5 As noted earlier, VECC's submissions on Smart Meters are provided in a separate section of this submission. However, to summarize, it is VECC's view that the OM&A costs associated with Smart Meters should be removed from the revenue requirement and recorded in Variance/Deferral Account #1556.

Shared Services

4.6 PUC is proposing a new Cost Allocation Methodology for Shared Services effective January 1, 2008. This methodology impacts not only the total costs PUC Servcies charges to PUC Distribution but also the split between operating and capital programs[24]. At the same time, the PUC Distribution's requirements for services from its affiliate are increasing in 2008. In response to VECC #18 a), PUC has indicated that the impact of the Cost Allocation Study is an increase of $175,728 in the costs allocated to PUC. This is equivalent to 6% of 2007 Shared Services costs. However, the response also indicates that the change in capitalization results in a $738,344 increase in costs charged to fixed assets and a

---

[20] OEB Staff Submissions, pages 6-7
[21] OEB Staff #13 and #14
[22] OEB Staff #14
[23] OEB Staff Submissions, pages 6-7

$562,616 decrease in the costs that will be charged to OM&A.

4.7 The balance of the 2007-2008 variance {$384,663 (14%)} is due to changes in actual costs incurred by PUC Services. PUC Distribution explains that this increase is due to increased use of vehicles, the implementation of upgraded software, wage increases and the addition of two new shared staff positions[25].

4.8 VECC does not have any specific submissions regarding these changes. However, the overall OM&A variance explanation provided by PUC in response to OEB Staff #4 b), shows a $192,000 reduction in the joint cost allocated to OM&A as a result of the Study. In contrast, the Admin Allocation reduction shown in response to VECC #18 a) is materially larger – particularly if one excludes the allocation to fixed assets. VECC invites PUC to reconcile these differences in its reply submission so that the Board has a consistent picture as to the impact of the proposed changes.

Taxes

4.9 In its submission Board Staff invites parties to comment on PUC's proposal to not deduct its excess interest expense for purposes of calculating PILs[26]. It is VECC's understanding that the Board has already addressed this issue in its EB-2007-0723 Decision regarding PUC's 2007 rates.

4.10 VECC notes that in response to VECC #21, PUC has updated its CCA calculations for 2008 to reflect the impact of the March 2007 Federal budget. VECC submits that these revised values should be used in PUC's 2008 PILS calculations.

---

[24] Exhibit #4,page 26
[25] OEB Staff #8
[26] OEB Staff Submissions, page 29

5 Cost of Capital/Capital Structure

5.1 VECC notes that the Capital Structure and Cost of Capital proposed by PUC is consistent with the direction of the Board in its Report on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors and the Board's recently issued Guidelines on cost of debt for 2008. VECC has no further submissions on this topic.

6 Deferral and Variance Accounts

New Deferral Accounts Requested

6.1 PUC has requested[27] three new deferral/variance accounts related to:

- MDMR (Meter Data Management Repository)
- Future Capital Expenditures and Projects
- Smart Meter Return and Distribution Expenses for 2009 and 2010.

6.2 The issues being addressed by the first two accounts are not unique to PUC but are issues/costs that could impact all electricity distributors in the Province. However, in each case it is not clear – at this point in time – whether a deferral/variance account will be required to address the related matter. In VECC's view it is pre-mature to approve these deferral/variance accounts at this point in time. Should the need arise, the Board can authorize the creation and use of such accounts on an industry wide basis and establish a common set of rules for use of the accounts at that time. VECC submits that for issues such as those identified above this is the best way to approach the matter, as opposed to on a piece-meal utility by utility basis.

6.3 Also, while the Application itself states that the account is for capital work during non-rebasing years (i.e., post 2008)[28], PUC's response to Staff #45 g) would

[27] Exhibit #1, page 31
[28] Exhibit #1, page 31

appear to suggest that the account is also meant to address over/under forecasting of 2008 capital costs. VECC submits that there is no basis/rationale for providing such an account for 2008 spending. Such spending should be addressed in the Application itself.

6.4 With respect to the Variance account for 2009 and 2010 Smart Meter Capital costs, should the Board adopt VECC's recommendations with respect to the treatment of Smart Meters for 2008 such a (new) account will not be necessary. PUC can continue to use the existing Smart Meter variance accounts (#1855 and #1856).

Balances in Existing Accounts

6.5 VECC notes the concerns by Board Staff regarding the balance in Account #1590 and related Regulatory Asset accounts. In VECC's view any questions regarding the appropriateness of the balances (including interest calculations) need to be resolved before they are disposed of.

Account #1590

6.6 In its Application, PUC is proposing to clear the forecast April 30, 2008 balance in Account #1590[29]. VECC submits that this approach is inconsistent with the Board's Phase 2 Decision regarding the Recovery of Regulatory Assets. In that Decision, the OEB stated that any residual in Account #1590 would be cleared after April 30, 2008.

Rate Riders

6.7 VECC notes that in response to VECC #22 d) PUC has corrected the allocation factors to be used for Accounts #1584 and #1548. These revisions should be reflected in PUC's final rates.

[29] VECC #22

7 Smart Meters

Regulatory Treatment

7.1 PUC has indicated that it plans to deploy 32,150 smart meters in 2008[30]. Accordingly, it has included in its 2008 capital spending the capital costs of this initiative[31]. Similarly in its OM&A costs, VECC has included the operating expenses associated with the smart meters[32]. The overall impact on the 2008 revenue requirement is $767,022[33]. However, to date, PUC has not been authorized to undertake smart metering activities[34].

7.2 As a result, VECC believes it is premature for the Board to approve a revenue requirement that assumes a significant deployment of Smart Meters by PUC in 2008. Rather, VECC submits, PUC should continue to use Accounts #1555 and #1556 to record any Smart Meter expenses and the Board should approve a Smart Meter rate adder for 2008 – the revenues from which would also be tracked in Account #1555.

Smart Meter Costs

7.3 The 2008 capital spending on Smart Meters includes investments in computer hardware and software[35]. VECC submits that, in its determination of the Smart Meter rate adder, the Board should direct PUC to calculate the applicable PILs assuming these expenditures attract the appropriate CCA rates (i.e., should not all be assigned to Class 47).

Rate Adder

---

[30] VECC #10 d)
[31] VECC #10 a)
[32] OEB Staff #43
[33] VECC #18 i)
[34] VECC #2 a)
[35] VECC #24

7.4 Consistent with the regulatory treatment of smart meters recommended above, VECC submits that the Board should approve a Smart Meter Rate adder and continued use of the related deferral/variance accounts for 2008. In VECC's view this approach will hold the utility harmless for smart meter costs, while recognizing that it has not yet received approval to proceed with smart meter deployment.

7.5 If the Board adopts VECC's recommended approach, the remaining question is to establish an appropriate level for the smart meter rate adder. The major advantage to the rate adder approach is that while the level of adder is important in terms of its impact on customer's bills and PUC's cash flow, at the end of day the Smart Meter Deferral/Variance accounts ensure that both PUC and customers are held harmless.

7.6 In the evidence provided to date[36], PUC has set out the 2008 costs (OM&A and capital-related) associated with Smart Meters and calculated a "rate adder". PUC should be directed to revise its calculated Smart Meter Rate Adder for 2008 so as to reflect the PILS changes reference above as well as the credit current balance in Account #1555[37].

7.7 In VECC's view the setting of appropriate Smart Meter rate adder should be a two step process. First, the correct rate adder should be established assuming all PUC's smart meters are deployed in 2008. Then, this value should be discounted to recognize the uncertainty associated with PUC actually being authorized and able to complete deployment of its smart meters by the end of 2008. As to the appropriate "discount factor" while it is a matter of judgement VECC submits that the rate adder should be set at somewhere between 50% and 75% of the annual cost associated with full deployment in 2008.

8 <u>Cost Allocation</u>

[36] VECC #18 i)
[37] VECC #1 c)

8.1 PUC has provided the Revenue to Cost ratios (RCR) resulting from its 2006 Cost Allocation informational filing[38]. Based on these results and the Board's November 2007 Guidelines, the customer classes requiring rebalancing are the Street Lighting and Sentinel Light classes where the RCR's are below the Guidelines and the GS<50 kW class where the RCR's are above the Guidelines. Furthermore, while within the Guidelines, the GS>50 kW class' RCR is also significantly above 100%.

8.2 In its Application, PUC proposed to rebalance the revenue requirement allocation between classes so as to address all of the aforementioned issues[39]. However, VECC has a number of concerns with PUC's "proposed" Revenue to Cost ratios. First, the Sentinel Lighting ratio is only increased from 38% to 40%. This change of two-percentage points is less than the increase proposed for the Residential class which already meets the OEB Guidelines. Compounding this concern is the fact that the Sentinel Lights are actually owned by PUC Energies Inc. - an affiliate of PUC Distribution.

8.3 One could legitimately argue that, under the requirements of the ARC, the RCR should be 100%. However, based on earlier Board Decisions regarding 2008 rates[40], VECC submits it would be reasonable to increase this RCR to at least 54%, with a direction from the Board that the RCR be increased in significant amounts on a yearly basis until it is within the acceptable range (i.e., half way to the low end of the range set out in the Board's Guidelines, with step increases in 2009 and beyond to get the RCR within the acceptable range). A similar issue exists for Street Lights, although in this case the proposed RCR only needs to be revised from 40% to 44% in the first "step".

8.4 VECC notes that in determining its revenue allocation by customer class PUC has used revenue at current (2007) rates that includes the smart meter rate adder[41]. Should the Board adopt VECC's recommendation for a separate smart meter rate

[38] Exhibit 8, page 9
[39] Exhibit 8, page 9
[40] EB-2007-0710 for Oshawa PUC Networks, page 46
[41] VECC #24 b)

adder then the revenue allocation would have to start with revenues at current rates excluding the smart meter rate adder. This would reduce the percentage revenue allocation to the Residential class required to achieve a 90% RCR. Offsetting this is the fact that the Residential class will attract a higher portion of Smart Meter costs when they are treated as a rate adder (and allocated per customer) than when they are included in the base distribution revenue requirement as proposed by PUC.

9 Rate Design

9.1 PUC's proposed fixed charge for Residential customers falls within the range of results generated by the Cost Allocation Informational filing[42].

10 Retail Transmission Service Rates

10.1 VECC shares Board Staff's concerns[43] regarding the proposed retail transmission service rates and submits that the current rates should be reduced by at least 18% - equivalent to the reduction in the Transmission Network charges.

[42] Exhibit 8, page 10
[43] OEB Staff Submissions, pages 27-28

11 Recovery of Reasonably Incurred Costs

11.1 VECC submits that its participation in this proceeding has been focused and responsible. Accordingly, VECC requests an award of costs in the amount of 100% of its reasonably-incurred fees and disbursements.

Respectfully Submitted on the 30th Day of March 2008

Michael Buonaguro
Counsel for VECC