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BY EMAIL

October 12, 2012

Ontario Energy Board
P.O. Box 2319
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2300 Yonge Street
Toronto ON M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Kenora Hydro Electric Corporation Ltd.
2012 IRM3 Distribution Rate Application
Board Staff Submission
Board File No. EB-2011-0177

In accordance with the Notice of Application and Hearing, please find attached the Board Staff Submission in the above proceeding.

As a reminder, Kenora Hydro Electric Corporation Ltd.'s Reply Submission is due by October 22, 2012.

Yours truly,

Original Signed By

Daniel Kim
Analyst, Applications & Regulatory Audit

Encl.

Ontario

ONTARIO ENERGY BOARD

STAFF SUBMISSION

2012 ELECTRICITY DISTRIBUTION RATES

Kenora Hydro Electric Corporation Ltd.

EB-2011-0177

October 12, 2012

Board Staff Submission
Kenora Hydro Electric Corporation Ltd.
2012 IRM3 Rate Application
EB-2011-0177

Introduction

Kenora Hydro Electric Corporation ("Kenora Hydro") 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 dsitribution rates that Kenora Hydro charges for electricity distribution, to be effective May 1, 2012. The Board put the application in abeyance until such time as Kenora filed evidence in support of the disposition of Account 1562 – Deferred PILs. Kenora Hydro filed the evidence related to the disposition of Account 1562 on July 18, 2012 and requested an effective date of October 1, 2012 for this element of its application. The Application is based on the Board's guidelines for 3rd Generation Incentive Regulation Mechanism.

In the interrogatory phase, Board Staff identified certain discrepancies in the data entered in the application model by Kenora Hydro. In response to Board staff interrogatories which requested either confirmation that these discrepancies were errors or, an explanation supporting the validity of the original data filed with the application, Kenora Hydro confirmed that there were errors and also provided an updated 2012 IRM Rate Generator Model (the "Model"). Board Staff also confirmed that it will make the necessary corrections to Kenora Hydro's supplementary models at the time of the Board's Decision and Order on the application.

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 Kenora Hydro.

Board staff makes submissions on the following matters:

- Disposition of Group 1 Deferral and Variance Accounts as per the *Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report");
- Account 1521 – Special Purpose Charge ("SPC");

- Revenue-to-Cost Ratio Adjustments;
- Lost Revenue Adjustment Mechanism (“LRAM”) Claim;
- Account 1562 – Deferred PILs; and
- Effective Date of the Rate Change.

DISPOSITION OF GROUP 1 DEFERRAL AND VARIANCE ACCOUNTS AS PER THE EDDVAR REPORT

Background

The EDDVAR Report provides that during the IRM plan term, a 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.

The December 31, 2010 actual year end amount for Group 1 accounts with interest projected to April 30, 2012 is a credit balance of $134,080. Credit balances are amounts refundable to customers. This amount results in a total claim of $0.00123 per kWh, which exceeds the preset disposition threshold. Kenora Hydro proposed to dispose of this credit balance over a one-year period.

Submission

Board staff has reviewed Kenora Hydro’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 *Reporting and Record-Keeping Requirements*. Board staff therefore submits that the principal balance should be disposed of on a final basis. Board staff also submits that the carrying charges should be updated at a later date to reflect the implementation date of the Board Decision and Order.

Board staff also notes that Kenora Hydro’s request for a one-year disposition period is consistent with the guidelines outlined in the EDDVAR Report with respect to the standard disposition period for Group 1 accounts (i.e. one year).

ACCOUNT 1521 – SPECIAL PURPOSE CHARGE ("SPC")

Background

In its Manager's Summary, Kenora Hydro did not request the disposition of Account 1521 since collections were in progress during 2011.

In response to Board staff interrogatory #5, Kenora Hydro completed the table below. Kenora Hydro also confirmed that the balances presented in the table below were subject to the annual financial statement audit for both 2010 and 2011. Kenora Hydro noted that the forecasted carrying charges for 2012 have not been audited.

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 Balance	Amount recovered from customers in 2011	Carrying Charges for 2011	December 31, 2011 Year End Principal Balance	December 31, 2011 Year End Carrying Charges Balance	Forecasted Carrying Charges for 2012 (Jan 1 – Oct 31)	Total for Disposition (Principal & Carrying Charges)
$42,745	$25,400.92	$0	$17,344.08	$0	$14,433.39	$83.51	$2,910.69	$83.51	$35.66	$3,029.86

Submission

Board staff has no concerns with the balances in Account 1521 presented by Kenora Hydro. Board staff submits that the Board should authorize the disposition, on a final basis, of Account 1521 as of December 31, 2010, plus the amount recovered from customers in 2011, including carrying charges as of the implementation date of the Board's Decision and Order. Board staff further submits that consistent with the disposition period for Group 1 Accounts, a disposition period of one-year should be authorized

REVENUE-TO-COST RATIO ADJUSTMENTS

Background

As directed by the Board in Kenora Hydro's 2011 cost of service proceeding (EB-2010-0135), Kenora Hydro adjusted its revenue-to-cost ratios for the Unmetered Scattered Load rate class from 138% in 2011 to 129% in 2012. The revenue shortfall would be recovered from the General Service > 50 kW rate class.

Submission

Board staff submits that the proposed revenue-to-cost ratio adjustments are in accordance with the Board's decision in Kenora Hydro's 2011 cost of service proceeding (EB-2010-0135).

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 for programs implemented prior to 2011.

Kenora Hydro originally sought to recover a total LRAM claim of $80,961.95 over a one-year period beginning October 1, 2012. The lost revenues include the cumulative effect of CDM programs implemented from 2006 to 2010. In response to interrogatories from Board staff and VECC, and upon receipt of final 2006-2010 OPA program results, Kenora Hydro updated its application. Kenora Hydro now seeks recovery of a total LRAM claim of $76,083.90, as well as $2,938.44 in carrying charges, for a total claim of $79,022.34 for the 2006 to 2010 period.

Submission

2006-2010 lost revenues

Kenora Hydro has requested the recovery of an LRAM amount that includes the cumulative effect of CDM programs implemented from 2006 to 2010. Kenora Hydro noted in response to VECC interrogatory 1(c) that it had not sought to recover historical LRAM amounts in its 2011 cost of service application (EB-2010-0135) as it was trying to mitigate the rate increases experienced by its customers as a result of the 2011 COS application.

Board staff notes that Chapter 2 of the *Filing Requirements for Transmission and Distribution* ("Filing Requirements") applications dated June 22, 2011, stated as follows:

> Distributors intending to file an LRAM or SSM application for CDM Programs funded through distribution rates, or an LRAM application for CDM Programs funded by the OPA between 2005 and 2010, shall do so as part of their 2012 rate application filings, either cost-of-service or IRM. If a distributor does not file for the recovery of LRAM or SSM amounts in its 2012 rate application, it will forego the opportunity to recover LRAM or SSM for this legacy period of CDM activity.

Board staff submits that Kenora Hydro has followed the process outlined in the Chapter 2 of the Filing Requirements and the CDM Guidelines when calculating its LRAM amount. Board staff submits that the lost revenues claimed in this rate application for 2006 to 2010 CDM programs are reasonable and have not been recovered in past applications by Kenora Hydro. Board staff supports the recovery of a principal balance of $76,083.90 by Kenora, which is the full LRAM principal amount requested.

Board staff notes that Kenora Hydro has requested its new rates to be effective October 1, 2012. Board staff submits that the carrying charges should reflect the implementation date of the Board's Decision and Order.

ACCOUNT 1562 – DEFERRED PILs

Background

Kenora Hydro filed its evidence related to the disposition of Account 1562 – Deferred PILs dated July 18, 2012. The PILs evidence filed by Kenora Hydro in this proceeding includes tax returns, financial statements, Excel models from prior applications, calculations of amounts recovered from customers, SIMPIL[1] Excel worksheets and continuity schedules that show the principal and interest amounts in the Account 1562 Deferred PILs balance. In pre-filed evidence Kenora Hydro applied to refund to customers a credit balance of $134,264 consisting of a principal credit amount of $112,909 plus related carrying charges of $21,355.

1 Spreadsheet implementation model for payments-in-lieu of taxes

After reviewing and answering Board staff interrogatories, Kenora Hydro filed revised SIMPIL models, a PILs continuity schedule and a final balance for disposition in its responses. The final balance did not change. Kenora Hydro is requesting to dispose a credit balance of $134,264 including related carrying charges up to September 30, 2012 over a 31-month period commencing October 1, 2012 and ending on April 30, 2015.

Submission

Proxy Entitlements from October 1, 2001 to April 30, 2002

In its PILs 1562 continuity schedule, Kenora Hydro recorded its entitlement to the 2001 PILs proxy starting on October 1, 2001 and the 2002 PILs proxy on January 1, 2002. However, due to its amended applications for rate adjustments on February 4th, April 2nd and April 4th, 2002, the effective date of the 2002 rates including the 2001 and 2002 proxies was delayed to May 1, 2002 at the request of Kenora Hydro. Therefore, there is a question as to whether the Board-approved accounting guidance for distributors following the standard application timing should not apply.

Board staff submits that the PILs proxy should be pro-rated for the period from May 1, 2002 (the effective dates for 2002 rates) to March 31, 2004, or 23 months. The sum of the 2001 PILs proxy of $55,592 and the 2002 PILs proxy of $158,629 is $214,221. The rates were determined based on a twelve month rate year which implies a monthly PILs proxy amount of $17,852 ($214,221/12) for the period from May 1, 2002 to March 31, 2004, or 23 months. Using this monthly entitlement, the total for the period shown is $410,590 ($17,852 x 23). Kenora Hydro has shown recoveries of $401,014 for the same period of May 1, 2002 to March 31, 2004 in its continuity schedule. The monthly PILs proxy calculated above was used to determine the proxy amounts in this table.

Recoveries in Rate Period	Amount of Recoveries	PILs Proxy
2002 - billings for 8 months only	$132,198	$142,816
2003	$210,885	$214,224
2004 – Jan.1 – Mar. 31	$57,931	$53,556
Sum	$401,014	410,596

Kenora Hydro stated in its response to Board staff interrogatory #7 that:

> Kenora did not consider any changes to the recording of the variance account was necessary as the Board Decision on the 2001 and 2002 PILs proxy only referenced the correction of an overstatement.
>
> Kenora does not agree with the Board staff's calculation as Kenora Hydro is of the opinion it properly calculated the 2001 and 2002 PILs proxy in its original application.[2]

Board staff notes that Kenora Hydro's comments above refer to the Board's 2002 decision and rate order which did not address the methodology of Account 1562 Deferred PILs. The Board's findings in EB-2008-0381, and in several decisions thereafter, have outlined the Board's views on methodology.

Board staff recognizes that the methodology is only a partial true-up of PILs actually paid. Kenora calculated recoveries from its customers to be $647,193.[3] However Board staff notes that during the period 2001 through 2005, Kenora paid no income tax PILs. As at December 31, 2005, Kenora had a remaining tax loss carry-forward balance of $273,129 to shelter taxable income for the tax years after 2005.[4]

Board staff submits that the proxy recognition recorded in the Account 1562 PILs continuity schedule should be based on the number of months between May 1, 2002 and the next rate change approved by the Board that Kenora implemented on April 1, 2004[5] which will result in a lower proxy that reflects the number of months of collection from ratepayers. Board staff submits that the alternative proffered by Board staff of calculating the PILs proxy with effect from May 1, 2002 is equitable to the ratepayers and to the shareholder. This alternative is consistent with decisions already made by the Board.[6]

Board staff requests that Kenora Hydro file a revised PILs continuity schedule with pro-rated PILs proxy entitlements from May 1, 2002 and final balance in Excel format as an alternative scenario for the Board to consider. Board staff also requests that in its Reply Submission that Kenora Hydro provides updated rate rider calculations using an

2 Responses to Board Staff Interrogatories, September 25, 2012, Pages 13-15.
3 Excel Workbook/ ED Disposition 1562 Balance IR 2012 09 25.xls
4 Application/ 2005 T2 tax return, Sch. 4 Loss Continuity/ PDF pages 487-491.
5 RP-2004-0058/ EB-2004-0044, Decision and Order, Interim Rates, March 12, 2004.
6 Board Decisions: North Bay, EB-2011-0187; Thunder Bay, EB-2012-0212; St. Thomas, EB-2012-0248.

effective date of November 1, 2012.

Billing Determinants used in the PILs Recovery Worksheets

Board staff noted that in the original application, the PILs recoveries were lower than one would expect compared to the PILs proxies in rates in 2002 and 2003. The trend for the majority of distributors is that the PILs recoveries exceed the proxies for the full years of 2003, 2004 and 2005. Board staff asked Kenora Hydro in interrogatory #9 to explain why the volumes shown as billed in 2002 are much lower than pro-rated actual volumes for the entire 2002 year.

Kenora Hydro responded:

> Kenora customers are in a climate where the billings for the first quarter of any given year are disproportionately higher than the rest of the year. We are a winter peaking utility, and as can be seen from this data, December through March are the coldest, highest heating degree months of the year.
>
> Actual billing reports were generated for the period May to December 2002, the consumption data as presented in the IRM is accurate.[7]

Board staff also asked Kenora Hydro to explain why the PILs recoveries were low within the 2003 recovery period.

Kenora Hydro responded:

> A very basic analysis of the changes in counts and consumption from the 2001 year of PILs proxy setting to the 2003 actuals reveals the resulting “under- recovery” in 2003.

7 Responses to Board Staff Interrogatories, September 25, 2012, Pages 18-19.

Class	2001 Count	2003 Count	Change	$ Impact on Collections
Residential	4,742	4,834	92	$1,683
GS Under 50 kW	760	731	(29)	$(1,011)
Unmetered SL	0	3	3	$104
GS Over 50 kW	66	59	(7)	$(3,518)
Streetlight	562	550	(12)	$(74)
Reduction in "Fixed" component of PILS Collection				**$(2,816)**

Class	2001 kWh or kW	2003 kWh or kW	Change	$ Impact on Collections
Residential	38,841,696	40,297,068	1,455,372	$1,392
GS Under 50 kW	27,984,272	27,846,286	(137,986)	$(56)
Unmetered SL	0	182,271	182,271	$74
GS Over 50 kW	119,070	102,696	(16,374)	$(1,955)
Streelight	5,094	5,244	(150)	$(44)
Reduction in "Variable" component of PILs Collection				**$(589)**

Total "expected" approximate decrease in 2003 collections over 2001 estimates: $(3,405).[8]

Board staff accepts Kenora Hydro's explanation.

Board staff submits that the statistics utilized in the PILs recovery calculations appear to be reasonable and consistent with the appropriate 2002-2006 historic billing determinant statistics as filed in Kenora Hydro's 2006 EDR model.

Excess Interest True-up

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 the TAXCALC worksheet as an extra deduction in the true-up calculations.

In determining the excess interest true-up variances in the SIMPIL models, the Board-approved maximum deemed interest of $222,523 was deducted from actual interest expense. To be consistent with past Board decisions, Kenora Hydro excluded interest on customer deposits and any effects on interest expense due to regulatory assets and liabilities. Kenora Hydro also confirmed that the IESO prudential was a GIC purchased with cash and that there were no fees or charges associated with the prudential. These

8 Responses to Board Staff Interrogatories, September 25, 2012, Pages 19-20.

changes to interest expense did not alter the excess interest true-up calculations since Kenora Hydro's total interest expense was less than the maximum deemed interest for each year from 2001 to 2005.

Board staff submits that there are no issues concerning the interest expense true-up calculations submitted by Kenora Hydro.

Income Tax Rates Used in SIMPIL Models Sheet TAXCALC

Kenora Hydro used the minimum income tax rates as shown on page 17 of the Board's combined proceeding decision for the purpose of true-up calculations. Kenora Hydro's rate base was $6,138,557 for the applications in 2001 through 2005.

Board staff submits that the minimum income tax rates as submitted by Kenora Hydro are appropriate based on its evidence.

EFFECTIVE DATE OF THE RATE CHANGE

Board staff submits that at issue in this Application is the effective date of the new distribution rates resulting from the Application of the price cap adjustment index.

Board staff notes that Kenora Hydro did not request that the Board declare its current rates interim, effective May 1, 2012 in the event that the Board's Rate Order would not be issued By May 1, 2012. As a result, Board staff submits that the new distribution rates cannot be effective May 1, 2012 since this would amount to retroactive ratemaking. Board staff therefore submits that the new rates be effective on the month following the issuance of the Board's Decision and Order on this application.

All of which is respectfully submitted