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Delivered by Courier and E-mail

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Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, Ontario M4P 1E4

Dear Ms. Walli:

Re: Peterborough Distribution Inc. - Request for change in 2007 electricity distribution rates reflecting reduced customer numbers, and amended 2008 IRM Model reflecting proposed revised 2007 rates

Introduction:

We are counsel to Peterborough Distribution Inc (“PDI”) in the above-captioned matter. On April 30, 2007, the Ontario Energy Board (the “OEB” or the “Board”) issued its Decision and Order in respect of PDI’s 2007 Electricity Distribution Rate (“EDR”) adjustment application (OEB File No. EB-2007-0571). That application was prepared and filed based on the OEB’s mechanistic adjustment process for 2007 rates.

On October 30, 2007, PDI filed its 2008 EDR application, for rates that will come into effect on May 1, 2008. This application used the approved 2007 distribution rates from EB-2007-0571 as a starting point to determine the 2008 distribution rates.

During the process of preparing its 3rd quarter 2007 financial statements, PDI management became aware that the distribution revenues would fall short of the forecast. The analysis conducted on the September 30, 2007 results revealed that 2007 revenue was below budget by approximately 4%, which represented approximately \$400,000 in distribution revenue for PDI. A detailed investigation into this issue determined that the customer numbers used in PDI’s 2006 EDR model were incorrect. Specifically, the number of unmetered sentinel lights was double-counted in numerous instances. The correct number of sentinel light connections (626) was included in the Sentinel Light class, but because customers with unmetered sentinel lights are in PDI’s Residential, GS < 50 kW and GS > 50 kW rate classes, 156 sentinel light connections were included in those classes as well. The impact was the greatest in the GS > 50 kW rate class since the ratio of double-counted unmetered sentinel lights compared to the total number of customers in this class was the highest. With an actual customer count of 363 in the

GS > 50 kW customer class, the inadvertent addition of 77 unmetered sentinel light connections inflated the size of that customer class by approximately 21%.

The following table highlights PDI's 2006 Board Approved EDR customer/connection counts and the adjustments needed to address the double-counting of unmetered sentinel lights.

| Rate Class customer/connections | 2006 EDR | Adjustment | Revised Count |
|--|---------------------|-------------------|--------------------------|
| Residential | 27,496 | (3) | 27,493 |
| GS < 50 | 3,440 | (76) | 3,364 |
| GS > 50 | 440 | (77) | 363 |
| Large User | 2 | 0 | 2 |
| Sentinel lights | 626 | 0 | 626 |
| Street lights | 7,431 | 0 | 7,431 |

The effect of the double-counting is that PDI cannot meet its revenue requirement. Its rates were designed on the basis of the inflated customer numbers, so that when the double-counted sentinel lights are removed from the customer counts, PDI is not recovering enough from each of its customers in the affected classes to meet that revenue requirement. On November 28, 2007, PDI staff presented the results of their investigation to their Board of Directors and were instructed to proceed with an application to the OEB to adjust 2007 distribution rates and to reflect the revised rates in the 2008 rate application.

Accordingly, PDI respectfully requests the following Order from the OEB:

- (a) that the OEB adjust PDI's current (2007) distribution rates to reflect the updated customer/connection numbers as outlined in Appendix A, effective January 1, 2008; and
- (b) That the OEB accept the revised 2008 IRM model and electricity distribution rates accompanying this letter as Appendix B in substitution for PDI's 2008 IRM model and proposed electricity distribution rates filed on October 28, 2007.

The details giving rise to this request are discussed below.

PDI's Adjustment to 2007 distribution rates:

In order to address the issue of shortfall in the 2007 revenue, PDI conducted an investigation involving the following activities.

1. Trend data analysis;
2. Ontario Energy Board (OEB) Rate model and forecasting review;
3. Billing system review to ensure rates were correct and billing was being completed accurately;
4. Revenue tracking by Rate Class; and
5. Rate model data input review.

The results of PDI's analysis are set out below.

1. Trend Data Analysis:

An analysis of current year trend data and previous year trend data confirmed that PDI would not achieve the revenue forecast by year-end.

2. OEB Rate model and continuity forecasting review:

An extensive review of the rate forecasting methodology and the previous year's rate model results was performed. The analysis of the rate models involved reviewing the OEB approved 2006 EDR model and tracking the rate changes to the OEB approved 2007 Incentive Regulation Mechanism ("IRM") and the impacts on the newly released 2008 IRM model. There were no errors found in the rates or the revenue projections used from model to model.

3. Billing system review:

A detailed utility bill audit was performed. Sample invoices were extracted from all rate classes. The bills were then calculated manually to ensure that PDI's Utility Management System ("UMS") billing system was billing accurately. The rate tables were reviewed to ensure they matched the tariffs, rates and charges set out in the applicable OEB Decisions. The classes into which customers were placed were confirmed. The revenue flows from the UMS billing system to the general ledger revenue and regulatory variance accounts in the financial management system (the "FMS") were confirmed. This review resulted in the following findings:

- The audit confirmed that the correct rates are being billed;
- The audit confirmed that customers' bills are being calculated correctly;
- The audit confirmed that revenues from the UMS billing system are being captured in the correct general ledger accounts in the financial system; and
- The audit confirmed the revenue shortfall has not been caused by a process or procedure associated with the operation of the UMS system.

4. Revenue tracking by rate class:

Management analyzed the revenue recorded in the financial system by customer class and type (down to the individual elements) for the twelve-month period from June 1, 2006 to May 31, 2007 (corresponding to the 2006 rate year of May 1, 2006 to April 30, 2007). Actual data was used to avoid the risk of projection errors. The queries used to extract the data were tested through audit sampling techniques to ensure accuracy. These results were then compared with the elements in the OEB-approved 2006 EDR model. This analysis determined that the GS > 50 kW class revenues were approximately \$400,000 below expectations.

5. Rate model data input review:

The investigation then examined the details of PDI's 2006 EDR rate application specifically related to the inputs associated with the GS > 50kW class. Newly developed database queries were used to confirm the inputs. Through that investigation, PDI determined that the number of GS > 50kW customers used in the rate model was overstated. In the 2006 OEB EDR model, distribution revenue was allocated to various rate classes based on historical revenue proportions, then divided into two components – fixed and variable. The model then took the fixed revenue component and applied the following calculation:

$$\text{fixed monthly charge} = \text{fixed revenue component} \div (2004 \text{ customer/connection count} \times \text{twelve months})$$

to arrive at the monthly fixed distribution rate. A similar calculation was used for the variable rate:

$$\text{variable charge} = \text{variable distribution revenue} \div (2002\text{-}2004 \text{ average usage per customer} \times 2004 \text{ customer/connection count})$$

A detailed analysis of the process used to determine customers/connections used in the 2006 EDR model revealed that the result was overstated because of an error in the logic of that process. The process counted each customer with an unmetered sentinel light as two customers instead of one. Unmetered sentinel lights exist in the residential, GS < 50 kW and GS > 50 kW rate classes.

The following table was shown in the introduction, above, and is reprinted here for the OEB's convenience. As noted above, it highlights the 2006 Board Approved EDR customer/connection counts and the adjustments needed to address the double counting of unmetered sentinel lights.

| Rate Class customer/connections | 2006 EDR | Adjustment | Revised Count |
|--|---------------------|-------------------|--------------------------|
| Residential | 27,496 | (3) | 27,493 |
| GS < 50 | 3,440 | (76) | 3,364 |
| GS > 50 | 440 | (77) | 363 |
| Large User | 2 | 0 | 2 |
| Sentinel lights | 626 | 0 | 626 |
| Street lights | 7,431 | 0 | 7,431 |

The revised customer numbers were entered in PDI's Board Approved 2006 EDR model. Copies of the Board Approved 2006 EDR model and the revised 2006 EDR model are provided in Appendix C and Appendix D, respectively.

A comparison of PDI's 2006 Board Approved 2006 distribution rates and the revised 2006 distribution rates using the corrected customer numbers is set out in the following table:

| | 2006 Approved Monthly Service Charge (a) | 2006 Revised Monthly Service Charge (b) | % Change (c) ((b-a)/a) | Billing Units | 2006 Approved Vol. Charge (d) | 2006 Revised Vol. Charge (e) | % Change (f) ((e-d)/d) |
|------------------------|---|--|---------------------------------|------------------|---|--|---------------------------------|
| Residential | 11.69 | 12.14 | 3.85 | kWh | 0.0121 | 0.0126 | 4.13 |
| GS < 50 | 25.15 | 26.12 | 3.86 | kWh | 0.0083 | 0.0086 | 3.61 |
| GS > 50 | 215.83 | 223.92 | 3.75 | kW | 2.2787 | 2.3905 | 4.91 |
| Large User | 4,318.56 | 4,489.77 | 3.96 | kW | 0.9281 | 0.9494 | 2.30 |
| Sentinel lights | 0.82 | 0.85 | 3.66 | kW | 4.2813 | 4.4426 | 3.77 |
| Street lights | 0.73 | 0.76 | 4.11 | kW | 3.2417 | 3.3616 | 3.70 |

When the customer numbers are revised in the 2006 EDR model, both the monthly service charge and the volumetric charge are affected, since customer numbers are used to determine the level of consumption used to design both the fixed and volumetric rates. In addition, the consumption used for volumetric rates is also used to establish the cost of power in the 2006 EDR model, which in turn affects the level of the working capital in the rate base. Specifically, the reduction in customer numbers reduces the level of the consumption which in turn reduces working capital in the rate base. As a result the total revenue requirement is reduced by \$1,449 since the rate base is somewhat smaller.

In the next step of the process the revised 2006 distribution rates were entered into the 2007 IRM model. A copy of the approved 2007 IRM model and the revised 2007 IRM are provided in Appendix E and Appendix F, respectively.

A comparison of the 2007 Board approved distribution rates, and the proposed revised 2007 distribution rates to be effective January 1, 2008, is set out below:

| | 2007 Approved Monthly Service Charge (a) | 2007 Proposed Monthly Service Charge (b) | % Change (c) (b/a) | Billing Units | 2007 Approved Vol. Charge (d) | 2007 Proposed Vol. Charge (e) | % Change (f) (e/d) |
|------------------------|---|---|-----------------------------|------------------|---|---|-----------------------------|
| Residential | 11.79 ✓ | 12.25 ✓ | 3.90 | kWh | 0.0122 ✓ | 0.0127 ✓ | 4.10 |
| GS < 50 | 25.37 | 26.36 | 3.90 | kWh | 0.0084 | 0.0087 | 3.57 |
| GS > 50 | 217.77 | 225.98 | 3.77 | kW | 2.2992 | 2.4125 | 4.93 |
| Large User | 4,357.42 | 4,531.07 | 3.99 | kW | 0.9365 | 0.9581 | 2.31 |
| Sentinel lights | 0.83 | 0.86 | 3.61 | kW | 4.3198 | 4.4835 | 3.79 |
| Street lights | 0.74 | 0.77 | 4.05 | kW | 3.2709 | 3.3925 | 3.72 |

Bill impacts resulting from the move from PDI's current Board Approved 2007 rates to its proposed 2007 rates are shown in the following table:

| | | 2007 Rate Order (a) | 2007 Revised IRM (b) | \$ Impact (c) (b-a) | % Impact (d) (c/a) |
|-----------------------|---------------------|----------------------------|-----------------------------|----------------------------|---------------------------|
| Residential | 1,000 kWh | \$115.15 | 119.23 | 4.08 | 3.54 |
| | 2,000 kWh | \$222.85 | 233.10 | 10.25 | 4.60 |
| GS < 50 kWh | 1,000 kWh | \$121.76 | 127.74 | 5.98 | 4.91 |
| | 2,000 kWh | \$222.66 | 234.70 | 12.04 | 5.40 |
| | 5,000 kWh | \$525.33 | 555.56 | 30.23 | 5.75 |
| GS > 50 kW | 60 kW, 15,000 kWh | \$1,831.41 | 1,925.61 | 94.20 | 5.14 |
| | 100 kW, 40,000 kWh | \$4,126.92 | 4,374.23 | 247.31 | 5.99 |
| | 500 kW, 100,000 kWh | \$11,516.35 | 12,142.90 | 626.55 | 5.44 |

In the final step of the process, the revised 2007 distribution rates were entered into the OEB's 2008 IRM model. A copy of PDI's amended 2008 IRM model accompanies this letter as Appendix B.

Bill impacts resulting from the move from PDI's current Board Approved 2007 rates to its proposed 2008 rates are shown in the following table:

| | | 2007 Rate Order (a) | 2008 Amended IRM (b) | \$ Impact (c) (b-a) | % Impact (d) (c/a) |
|-----------------------|---------------------|----------------------------|-----------------------------|----------------------------|---------------------------|
| Residential | 1,000 kWh | \$115.15 | 112.66 | (2.49) | (2.16) |
| | 2,000 kWh | \$222.85 | 217.36 | (5.49) | (2.46) |
| GS < 50 kWh | 1,000 kWh | \$121.76 | 121.58 | (0.18) | (0.15) |
| | 2,000 kWh | \$222.66 | 221.15 | (1.51) | (0.68) |
| | 5,000 kWh | \$525.33 | 519.88 | (5.45) | (1.04) |
| GS > 50 kW | 60 kW, 15,000 kWh | \$1,831.41 | 1,824.26 | (7.15) | (0.39) |
| | 100 kW, 40,000 kWh | \$4,126.92 | 4,108.71 | (18.21) | (0.44) |
| | 500 kW, 100,000 kWh | \$11,516.35 | 11,387.62 | (128.73) | (1.12) |

PDI notes that the under-recovery resulting from the double-counting of customers in the Residential, GS<50 and GS>50 classes has occurred since prior to May 2006. However, PDI is not requesting that the OEB approve the recovery of any revenue forgone prior to

January 1, 2008. PDI simply wishes to correct this situation and ensure that it is able to recover its Board Approved revenue requirement from January 1, 2008 forward.

Summary:

In light of the foregoing, PDI requests that the OEB approve the proposed revised 2007 distribution rates effective January 1, 2008, and that these rates be incorporated in the amended 2008 PDI rate application. PDI submits the proposed distribution rates are just and reasonable on the following grounds:

- a) the proposed adjusted rates are necessary to meet PDI's Market Adjusted Revenue Requirement; and
- b) there are no impacts to any of the customer classes or consumption level subgroups that are so significant as to warrant the deferral of any adjustments being requested by PDI.

In order for the OEB to consider and address these requests, we ask that the OEB consider this letter as constituting PDI's application.

List of Appendices:

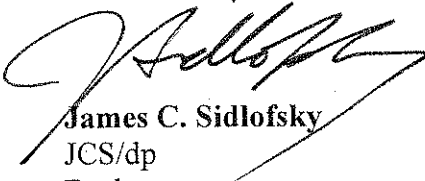
The following Appendices, referred to above, accompany this letter:

- Appendix A: Proposed revised 2007 Tariff of Rates and Charges
- Appendix B: Revised OEB 2008 IRM model
- Appendix C: OEB Approved 2006 EDR model
- Appendix D: Revised 2006 EDR model
- Appendix E: OEB approved 2007 IRM model
- Appendix F: Revised 2007 IRM model

We thank you for your assistance in this matter. Should you have any questions or require further information, please do not hesitate to contact me.

Yours very truly,

BORDEN LADNER GERVAIS LLP



James C. Sidlofsky
JCS/dp
Encl.

Copies to: Larry Doran, President & Chief Executive Officer, PDI
Andy Hoggarth, Vice-President & Chief Financial Officer, PDI
Rob Kent, Manager of Finance, PDI

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