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Ontario

BY E-MAIL

April 19, 2013

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Toronto Hydro-Electric System Limited ("THESL")
Board Staff Comments on Draft Rate Order
Board File Number EB-2012-0064

In accordance with the Board's Partial Decision and Order dated April 2, 2013, please find attached Board staff's comments on the draft Rate Order filed by THESL on April 12, 2013.

Original Signed By

Martin Davies
Project Advisor, Applications & Regulatory Audit

Attachment

cc: Parties to EB-2012-0064 proceeding

ONTARIO ENERGY BOARD

BOARD STAFF COMMENTS

-DRAFT RATE ORDER-

Toronto Hydro-Electric System Limited

EB-2012-0064

April 19, 2013

Introduction

On April 12, 2013, Toronto Hydro-Electric System Limited ("THESL") filed a draft Rate Order ("DRO") pursuant to the Ontario Energy Board's EB-2012-0064 Partial Decision and Order ("Decision") dated April 2, 2013.

Board staff's comments on the DRO follow.

Calculation of 2013 ICM Project Recovery

Board staff has a number of concerns with the approach THESL has used in making this calculation.

Board staff's understanding of THESL's approach, based on the DRO filing[1], is that this recovery is $218.53 million of ICM projects for 2013. The breakdown of this number is $387.15 million of 2013 approved in-service capital projects, less the threshold CAPEX of $166.19 million, less the 2013 Bremner expenditures of $2.43 million for which THESL is proposing a separate rate rider.

Approved Project Level

THESL's DRO states that the approved ICM project level, including the 2013 Bremner expenditures, is $220.96 million.[2] This number is shown in Table 1 and appears to be the Board Approved ISA (In-Service Additions), as determined by THESL for segments in the "B" category, but apparently excludes segments in the "C" category.

Board staff submits that THESL should clarify in its reply submission its basis for determining the approved ICM project level, specifically commenting on the apparent exclusion of "C" projects from the approved amount, and if so whether or not this implies that THESL will not go ahead with these projects and how such a determination was made.

[1] Toronto Hydro-Electric System Limited, EB-2012-0064, *Draft Rate Order,* Appendix C, Schedule 2, page 1 of 1
[2] P.5, L9-L14

"Normal Capital Budget"

THESL is using its "normal capital budget," which it defines as PCI, Pre-2012 CWIP and Board Approved Non-Material ICM as the Threshold CAPEX to calculate the approved project level in place of the ICM WorkForm calculated threshold. The "PCI" and "Board Approved Non-Material ICM" will be discussed in more detail subsequently. THESL characterized its "normal capital budget" as follows:

> During the IRM period, THESL's "normal capital budget" is the amount falling below the Board's ICM materiality threshold, as determined by the *Supplementary Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors,* dated September 17, 2008."[3]

Board staff notes that the Decision referred in a number of its findings to THESL's "normal capital budget" but is unclear as to how THESL reached the conclusion that the definition of this term is as described above since the referenced document does not appear to define a "normal capital budget" and the Decision also did not further define the term. The Board's Supplementary Report referenced by THESL above described the materiality threshold as below[4]:

[3] P.6, L1 –L3

[4] *Supplementary Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, S*eptember 17, 2008, p.33

Accordingly, the Board has determined that the appropriate CAPEX to depreciation threshold value to establish materiality for the incremental capital module should be distributor-specific and derived using the following formula:

$$\textit{Threshold Value} = 1 + \left(\frac{RB}{d}\right) * (g + PCI * (1 + g)) + 20\%$$

Where:

RB = rate base included in base rates ($);
d = depreciation expense included in base rates ($);
g = distribution revenue change from load growth (%); and
PCI = price cap index (% inflation less productivity factor less stretch factor).

Board staff notes that while THESL is stating that its "normal capital budget" is the amount falling below the Board's ICM threshold, THESL also appears to be stating[5] that it is not using the ICM WorkForm calculated Threshold CAPEX of $163.19 million, which is derived from the above formula, but instead the "normal capital budget" of $166.19 million, which is different from the Board threshold and is determined by THESL as described above. Board staff submits that THESL should clarify this matter in its reply submission.

Board Approved Non-Material ICM

THESL stated that in the Decision, the Board had found that several of THESL's proposed ICM segments are non-discretionary and otherwise satisfy the requirements for ICM treatment, but that the amount of funding requested in those segments was not significant in the context of THESL's overall capital budget and, accordingly, THESL could fund those segments through its normal capital budget during the IRM period.

THESL's DRO includes a 2013 in-service capital project amount of $5.72 million which is described as "Board Approved Non-Material ICM," or minor projects.

Based on the notes to Table 1, this amount appears to arise from segments B7, B8, B14, B16 and B18. The Board stated in its finding for segment B7 that "THESL should be able to fund this project through its normal capital budget

[5] DRO, App. C, Sch. 2, p.1

during the IRM period, and will not be permitted additional recovery for this project."[6] While the Board did not always use the identical wording for the other referenced segments, it made similar findings for them.

Board staff notes that the Decision also made similar findings for segments B15 and C3 which THESL has not included in its "Board Approved Non-Material ICM." This is summarized in the table below:

Board Disallowances For Minor Projects	
	$M
Included by THESL	
B7 Polymer SMD-20 Switches	0.93
B8 SCADA-Mate R1 Switches	0.87
B14 Stations Circuit Breakers	0.76
B16 Downtown Station Load Transfers	1.68
B18 Hydro One Capital Contributions	1.48
Sub Total	5.72
Excluded by THESL	
B15 Stations Control & Communication Systems	0.68
C3 Fleet Capital	0.76
Sub Total	1.44
Total	7.16

It is unclear to Board staff why THESL has excluded segments B15 and C3 from this amount and Board staff submits that THESL should state the basis for this exclusion in its reply submission.

Board staff is also concerned that THESL is including the amount of these projects in the 2013 in-service capital, along with other projects which the Board has approved. This means that THESL is increasing its level of 2013 project recovery by this amount, which appears to be contradictory to the Board's finding

[6] *Partial Decision and Order*, EB-2012-0064, p. 31

that THESL would not be permitted additional recovery for these projects. Board staff submits that THESL should provide further explanation of this approach in its reply submission.

Meaning and Treatment of "PCI" Projects

Appendix C, Schedule 2 of the DRO includes in addition to the item discussed above of "Board-Approved Non-Material ICM," an item "PCI" in the amount of $115.02 million. This appears to be the total Board Approved ISA of segments C1 to C4, plus Allowance for Funds Used During Construction. The term "PCI" does not appear to be defined in this context and also, as discussed earlier, it is not clear to Board staff why these segments are determined to be below threshold CAPEX, while the other segments are above.

Departure from ICM WorkForm Calculated Threshold CAPEX

The total of the above two items (i.e. PCI plus Board Approved Non-Material ICM) plus Pre-2012 CWIP, of $166.19 million is stated by THESL as being used to establish the projects eligible for ICM funding, instead of the ICM Workform calculated Threshold CAPEX of $163.83 million.

THESL does not appear to provide an explanation for this departure from normal practice. THESL removes this amount to determine the Incremental CAPEX used in the Incremental Capital Workform[7] and calculates the proposed rate riders on the basis of an amount of $218.53 million. Board staff submits that THESL should explain this approach in its reply submission.

Impacts of Board Staff Concerns

Board staff notes that if the Board Approved Non-Material ICM project amount as calculated by Board staff is removed from the approved projects and the ICM Workform calculated Threshold CAPEX is used instead of the alternative proposed by THESL, the 2013 Incremental CAPEX, or total project recovery drops from $218.53 million to $213.73 million, or almost $5 million, as shown in the table below:

[7] DRO, App. C/Sch. 3/p.12

THESL 2013 Incremental Capital CAPEX ($)	
THESL DRO App. C/Sch. 3/p. 12 of 16	218,527,329
Add back:	
THESL Proposed Threshold	166,191,897
Subtract:	
ICM Workform Calculated Threshold CAPEX	163,833,177
Board Disallowances for Minor Projects	7,160,000
Revised 2013 Incremental Capital CAPEX	213,726,049

Board staff invites THESL to comment in its reply submission as to why this amount, rather than the amount which it has proposed, is not the appropriate 2013 recovery amount.

<u>Tariff of Rates and Charges</u>

Board staff submits that THESL's proposed Tariff of Rates and Charges did not in a number of instances use the standard Board terminology and that these discrepancies should be addressed before the Final Rate Order is issued.

Board staff also has a number of other specific concerns:

1. THESL has included for the "Standby Power Service Classification" a "Regulatory Component" of Monthly Rates and Charges, which is not on its current Tariff of Rates and Charges. Board staff submits that THESL should explain the reason for this addition in its reply submission.

2. In the Streetlighting and Unmetered Scattered Load rate classes THESL has included some proposed rates of $0.00. Board staff submits that such rates should not be included on the final Tariff of Rates and Charges unless THESL can provide appropriate justification for them.

3. In Specific Service Charges, THESL has included two charges which are characterized as “Specific Charge for Access to the Power Poles $/pole/year” the first of which is for $22.35 and the second for $18.55. Board staff is of the view that the second charge should also contain the following bracketed term “(Third Party Attachment to Poles)” as is the case on THESL’s existing Tariff of Rates and Charges.

4. Where Loss Factors are concerned, THESL’s proposed Tariff of Rates and Charges includes a “Total Loss Factor – Secondary Metered Customer > 5,000 kW” of 1.1087 as compared to 1.0187 on THESL’s existing Tariff of Rates and Charges. Board staff is of the view that the number on the existing Tariff of Rates and Charges is the correct one.

Board staff submits that THESL should comment on these concerns in its reply submission.

<u>Deferral and Variance Accounts</u>

Carrying Charges

In its DRO,[8] THESL noted that the Board had approved the disposition of the Account 1562 PILs balance and that this approved balance included carrying charges up to April 30, 2012. THESL stated that consistent with the Board’s directions on carrying charge calculations on Account 1562, THESL had updated this amount to include carrying charges to December 31, 2012.

Board staff submits that THESL should update carrying charges on all deferral account balances to be disposed up to May 31, 2013, the date prior to implementation of the new rates.

Rate Riders

THESL further stated in its DRO regarding deferral and variance accounts that the provided DRO Tariff of Rates and Charges reflected a variable only rate rider. THESL acknowledged that the Decision had stated that THESL was to dispose

[8] DRO, p.10

of the approved balances in the 1521 and 1562 accounts through a combined fixed and variable Deferral/Variance Account Rate Rider. However, THESL noted that it had proposed clearance of these balances through a variable rate rider only, which was consistent with the treatment in the Board's IRM model. THESL stated that it was prepared to create a rate rider with both fixed and variable components (and had provided calculations using both approaches), but preferred to remain consistent with the Board's methodology for this account, primarily to minimize the already large number of rate riders and adders.

Board staff notes that the Decision had stated that "The Board finds that THESL is to dispose of this balance and the $6,979,536 credit balance in account 1562 using a combined fixed and variable DVA rate rider with a one-year recovery period."[9]

Board staff submits that since the Board's direction on this matter is clear that THESL should use a combined fixed and variable DVA rate rider, rather than a variable only rider as proposed.

Billing Determinants

Board staff notes that in calculating rate riders and RTSRs, THESL has used 2010 billing determinants as the basis for the allocation of balances to the rate classes, as well as for the basis of the calculation of the corresponding volumetric rate riders. Board staff further notes that in a typical IRM application, the most recent billing determinants are used as the basis for the allocation of balances and calculation of rate riders.

Board staff submits that as the Board is approving 2013 rates for THESL in this application, standard practise would require that the rate riders be based on 2011 billing determinants.

Board staff acknowledges that as THESL's application was filed near the RRR filing deadline for its 2011 billing determinants, the 2011 information may not have been readily available to THESL at that time.

[9] *Partial Decision and Order*, EB-2012-0064, p.70

Board staff notes that THESL's use of 2010 billing determinants, as opposed to 2011 billing determinants, would create a potential allocation issue. Board staff submits that THESL should address in its reply submission whether the use of 2011 billing determinants would result in a materially different allocation amongst each of the classes for the disposition of Deferral and Variance Account balances, shared tax savings, ICM revenue requirements and RTSRs approved by the Board.

Board staff would consider THESL's approach to be acceptable provided that it can show that the allocation between classes using 2011 billing determinants would not be materially different from that resulting from use of the 2010 billing determinants.

Board staff submits however that if the use of the 2011 billing determinants would result in a materially different allocation between rate classes, THESL should be required to recalculate all applicable rate riders using the 2011 billing determinants to be consistent with the Board's standard practise for IRM applications.

Appendix E Draft Accounting Order

THESL stated in the DRO[10] that,

> The Decision required THESL to specify the treatment of the rate rider revenues in the next rebasing application. THESL anticipates that at the time of rebasing, THESL will calculate the historical revenue requirement based on actual in-service additions of the ICM projects, and compare with revenues collected through the approved ICM rate riders. Any variances will be refunded/collected from customers through a rate rider to be cleared at a future date. THESL observes that this is similar to the method the Board used to reconcile Smart Meter rate rider revenues with Smart Meter capital spending.

Board staff has two issues with THESL's approach to the Draft Accounting Order, which are outlined below:

[10] DRO, pp.10-11

Clarity of the treatment for the rate rider revenues through a true-up of the revenue requirement for actual in-service assets

Board staff submits that THESL's treatment of the rate rider revenues should be more clear and detailed. The accounting order should specify that there will be a true-up of the (current) revenue requirement which was used to derive the rate rider revenues.

Accordingly, at the time of true-up, THESL should recalculate the revenue requirement impacts (using the Incremental Capital Workform) based on the actual in-service assets (used and useful) to determine the revenue requirement on an actual basis for each applicable period (e.g., 2013 and 2014). All other input information in the Incremental Capital Workform should remain unchanged (e.g., Return of Rate Base - Equity or Current Tax Rate).

The recalculated revenue requirement should then be compared to the rate rider revenues collected in the same period to determine the variances. These variances should be refunded to or collected from customers through a rate rider at the time of THESL's next rebasing application.

Accounting treatment of the revenue requirement impact of replaced assets which are concurrently in rate base with new in-service asset replacements

Board staff notes that THESL observed that its treatment of the rate rider revenues is similar to the method the Board used to reconcile smart meter rate rider revenues with Smart Meter capital spending. In this context, the Board may also wish to consider whether or not depreciation of assets coming out of service should be tracked for future consideration by the Board. Board staff notes that under the general framework of the accounting for smart meters, the Board's treatment does not allow for the "double counting" of the not in-service conventional meters (i.e., stranded meters) and the new smart meter replacements, which are concurrently included in rate base. Board staff invites THESL to comment on this matter in its reply submission.

- All of which is respectfully submitted-