CANADIAN NIAGARA POWER INC.
A FORTIS ONTARIO Company

June 27, 2013

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

Dear Ms. Walli:

RE: DEFINING AND MEASURING PERFORMANCE FOR ELECTRICITY DISTRIBUTORS (EB-2010-0379) "EMPIRICAL WORK IN SUPPORT OF INCENTIVE RATE SETTING IN ONTARIO" (THE "PEG REPORT"); CANADIAN NIAGARA POWER INC. ("CNPI") COMMENTS

Pursuant to the Board's letter dated May 30, 2013, the following are CNPI's comments relating to the PEG Report. Please find accompanying this letter two (2) copies of CNPI's comments relating to the above captioned matter. Coincidental with this written submission, CNPI has submitted an electronic copy through the Board's Regulatory Electronic Submission System.

CNPI's comments are limited to the Pacific Economic Group Research LLC ("PEG") characterization of CNPI as an "Above Average Customer Growth" LDC, and; second, the appropriateness of including Algoma Power Inc. ("API"), an affiliate of CNPI, in the analysis performed by PEG.

CNPI believes that it has been erroneously identified as an "Above Average Customer Growth" LDC, likely the result of an incomplete data set. The calculations were based on growth identified in PEG's supporting Excel Spreadsheet[1] "TFP and BM database calculations" Tab "Output Indexes". The data used by PEG in its analysis and detailed in the supporting spreadsheet noted here has been interpreted to be growth in the generic sense; that being new customer connections, increases in throughput and capital additions.

However, the increase in customers, throughput and capital determined for CNPI by PEG in 2003 is not actually growth in the generic sense but rather the result of acquiring the former Granite Power Distribution Corporation, the then electricity distribution company in the town of Gananoque, Ontario. This acquisition by CNPI became effective on April 1, 2003 and the LDC service territory was branded as Eastern Ontario Power ("EOP"); a service territory of CNPI. Until the harmonization of electricity distribution rates in its 2009 Electricity Distribution Rate application, EB-2008-0222 and EB-2008-0223, CNPI reported its Regulatory Reporting and Record Keeping Requirements ("RRR") data separately for EOP and its service territories in Fort Erie and Port Colborne.

[1] PEG_Working_Papers_PartII, Spreadsheet "TFP and BM database calculations", Tab "Output Indexes"

It is CNPI's understanding that the former electricity distribution company in Gananoque did not file any rate information with Ontario Hydro (Hydro One) after 1993, did not unbundle its electricity distribution rates in 2002 and did not report in accordance with the Board's RRR or Performance Based Regulation ("PBR") requirements. Therefore, with the information available to PEG to perform its analysis, PEG may not have had any evidence as to the existence of an LDC in Gananoque prior to CNPI's RRR submission in 2004.

CNPI filed a Rate Unbundling and Design ('RUD") application in June 2003 and received rates effective April 1, 2003. The most reliable data set for EOP is the 2006 EDR application, EB-2005-0346 which contains a full data set for 2004; the first full year of operation of the EOP service territory by CNPI.

For 2003, we reported (in the 2006 EDR application) the following customer counts and throughput:

Customer Class	Customer Count	Throughput in kWh
Residential	3,042	28,624,805
GS less than 50 kW	378	13,817,663
GS greater than 50 kW	34	42,435,353

These additional customers and throughput together with the acquired capital stock all appear as growth for CNPI in 2003 and results in PEG's characterization of CNPI as an "Above Average Customer Growth" LDC. CNPI submits that the PEG analysis of CNPI ought to be amended in a manner which appropriately considers the acquisition of EOP on April 1, 2003. Given the uncertainty surrounding data that may exist in the timeframe of 1993 to 2003, CNPI suggests that the most appropriate data set available to properly characterize EOP is the 2004 data set that was filed as part of the EOP 2006 EDR; 2004 was CNPI's the first full year of operation for EOP.

The second point CNPI wishes to highlight is the appropriateness of including API, an affiliate of CNPI, in the analysis performed by PEG. API's cost characteristics were accurately described in the Board's Decision in the matter of EB-2007-0744, an application by Great Lakes Power Limited (the predecessor to API) for an Order or Orders approving just and reasonable rates and other service charges for the distribution of electricity. In that Decision[2] the Board wrote;

> *"GLPL presents a unique challenge for the Board. In reviewing the record for this case and examining the history of this applicant before the Board it has become clear that conventional ratemaking practice cannot address the issues presented by this applicant.*
>
> *Conventional ratemaking cannot result in a rate that will cover the Company's costs, provide for a reasonable return on investment, while being reasonable from a ratepayer's point of view.*
>
> *This circumstance arises directly out of the characteristics of the Applicant's service area. The Applicant's service area is more than twice the area of the greater Toronto area. It has less than 12,000 customers and has the lowest customer/kilometer ratio in Ontario with only 6.7 customers per kilometer on average. 99.9% of its service area is rugged and sparsely populated wilderness. Its service area is characterized by long runs of distribution wire between customers.*
>
> *This is a high cost, low revenue service area."*

[2] Board Decision and Order, EB-2007-0744, dated October 30, 2008, page 3

API is unique in the way its distribution rates are set by the Board. Pursuant to O. Reg. 442/01, and with the exception of the Seasonal and Street Lighting Service Classifications, API's rates are adjusted in line with the average of any adjustment to rates approved by the Board for all other distributors for the most recent rate year. This mechanistic adjustment to electricity distribution rates for its residential and general service customer is essentially a disconnect or complete decoupling of inputs and outputs with respect to rate setting for API. The difference between Board approved revenue requirement and revenue derived from electricity rates is compensated by the Remote and Rural Rate Protection Plan ("RRRP"). Notwithstanding the fact that API is conscious of its operating costs and strives to find efficiencies in its operations, CNPI submits that this decoupling of inputs and outputs in the API rate design methodology renders the PEG econometric modeling of API inappropriate. Stated candidly, under the current rate setting scheme, O. Reg. 442/01, changes to API's operating costs have no direct correlation with changes to its electricity distribution rates. Changes to electricity distribution rates are a function of the changes in rates of all other LDCs. Within this realm, API ought to be in the average cohort of those LDCs contributing to the average rate adjustment determined annually by the Board for use in API's IRM applications.

Fairness to API is a matter of concern. In its most recent cost of service application, API had an approved revenue requirement of $20,198,813 of which $11,411,951 or 56.5% was RRRP funded. The manner in which rates are set and the RRRP funding amount is determined has been consistent since the Board's Decision in the matter of EB-2007-0744; failure to recognize the uniqueness of API and that fact that it is a high cost, low revenue service area in this effort to define and measure performance is unfair to API. API's costs are inherent to the characteristics of the service territory in which it operates; this vast territory and low customer density have no comparators within the balance of LDCs in Ontario. Failure to recognize these cost characteristics and the RRRP funding requirement renders API as an inferior cost performer. The inherent costs of operating in a high cost, low revenue service area combined with distribution rates that are indexed on the average of other LDCs in Ontario means that API is forever defined as an inferior cost performer. There will be no practical means available to API to improve its ranking and to be measured anything but an inferior cost performer despite any operational efficiencies it may achieve.

Further, the fairness to other LDCs of including API within the PEG analysis was discussed in the proceedings held on May 16th, May 27th and May 28th, 2013. In the proceeding held on May 16, 2013 Mr. Jay Shepherd, on page 127 of the transcript, raised the issue of fairness. Mr. Shepherd correctly pointed out that API's presence within the group skews the standard. Mr. Kaufmann agreed.

> MR. SHEPHERD: No, I am not asking the question about Algoma and Hydro One. I am asking the question about, for example, Bluewater in the same group with Algoma, which would then be put at a lower standard, in effect, because Algoma skews the standard.
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> DR. KAUFMANN: Right.

In this instance fairness extends to the LDCs other than API. As was recognized in the Board's Decision in the matter of EB-2007-0744, API is a high cost, low revenue service area. To recognize this fact, electricity distribution rates, unlike those of other LDCs, are governed by regulation and protected with the RRRP. The inclusion of API within a select group of LDCs will unduly favour those LDCs fortunate enough to be included in a grouping with API.

In summary there are two basic issues of fairness in play for API. First, electricity distribution rates for API are set in accordance with O. Reg. 442/01 and as a result there is a complete decoupling of input cost and electricity costs. This decoupling effectively negates the intent of the PEG econometric modeling. Second, API is a high cost low revenue LDC, this has been recognized in successive Board decisions beginning with EB-2007-0744. Including API within any cohort will artificially and unduly benefit other LDCs in that cohort.

CNPI submits that for these two reasons API ought to be excluded from this comparative process. In fairness, and as an alternative, API could be measured against itself. The Board could utilize the current analysis of API's costs as a benchmark and measure future performance against this benchmark value as an indicator of performance and efficiency. This solution places API in a cohort of its own, is fair to API and does not unduly benefit others.

CNPI thanks the Board for this opportunity to comment on the PEG Report.

Yours truly,

Original Signed by:

Douglas Bradbury P.Eng,
Director Regulatory Affairs