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January 17, 2014

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

Dear Ms. Walli:

RE: 2014 ELECTRICITY DISTRIBUTION RATE APPLICATION FOR ALGOMA POWER INC. ("API") – EB-2013-0110
INTERROGATORY RESPONSES

Please find accompanying this letter two (2) copies of API's responses to the interrogatories submitted by Board Staff on Supplementary Evidence.

A PDF version of these responses will, coincidently with this written submission, be filed via the Board's Regulatory Electronic Submission System.

If you have any questions in connection with the above matter, please do not hesitate to contact the undersigned at (905) 994-3634.

Yours truly,

Original Signed by:

Douglas R. Bradbury
Director, Regulatory Affairs

Enclosures

1-Staff-1s

1. Please provide a response to each of the questions below for both of the following time periods: i) Between the time of Fortis' acquisition of Algoma and the Board's 2012 IRM Decision, and ii) Since the time of the Board's decision on API's 2012 IRM application in which the Board denied API's request for a change to its stretch factor assignment.
   a. Which, if any, of the service territory characteristics and/or business conditions identified in API's evidence and reply submission have changed? Please explain how, when, and why.
   b. What negative economic circumstances have occurred?
   c. How has API's business risk changed?

Preamble

Board staff's interrogatory seems to place great emphasis on the Board's 2012 IRM Decision (EB-2011-0152) in regard to API's stretch factor assignment (the "2012 Decision"). It is important to note that the third generation IRM ("3GIRM") stretch factor methodology on which the 2012 Decision was based was different from the fourth generation IRM ("4GIRM") stretch factor assignment methodology applicable to API's current 2014 IRM application. Under 3GIRM, stretch factors were established based on OM&A costs relative to other LDCs. Under 4GIRM, stretch factors are established based on costs relative to each LDC's costs as predicted by an econometric model. As set out in API's response to interrogatory #7, API does not believe that the econometric model is responsive to API's unique attributes.

In API's 2012 third generation IRM application (i.e. the subject of the 2012 Decision), API had proposed to apply the mid-point stretch factor following consultations with the intervenors of record to develop a rate-setting methodology satisfying both IRM and RRRP requirements. At that time, API felt that the methodology used to assign stretch factors in the 3GIRM did not adequately reflect API's attributes. The Board denied API's request, citing amongst other things, that an IRM application was not the appropriate venue in which a change in stretch factors should be considered. Subsequently, in API's 2013 IRM application also filed under 3GIRM, API respected the Board's 2012 Decision on this matter by proposing the same stretch factor assignment required by the Board in the 2012 Decision.

Now, in API's first 4GIRM application, API has responded to the Board's invitation set out in its Report dated September 6, 2013, to claim extenuating circumstances for specific stretch factor assignment treatment

The Board's decision to deny API's proposed stretch factor assignment in the 2012 Decision was based on an entirely different stretch factor assignment methodology than that used under 4GIRM. Therefore, API is having difficulty recognizing the relevance of the 2012 Decision in regard to API's proposed stretch factor assignment in its current 4GIRM application.

Response:

a. None of the service territory characteristics and/or business conditions identified in API's evidence and reply submission has changed materially.
b. API's service territory has experienced the effects and has faced the challenges of the recent economic downturn similar to much of Ontario.

c. In the absence of a definition offered by Board staff, API interprets business risk to be the ability to retain load, the ability to provide safe and reliable service, the ability to collect revenue, and the ability to manage costs at a level that the regulator will approve for recovery in rates. From this perspective, API's business risk has not changed.

1-Staff-2s

2. Please provide any quantitative analysis that supports API's claim that it should be in a stretch factor group other than the lowest ranked group.

Response:

In its response to Board staff Interrogatory No. 4, API has provided quantitative analysis that supports API's claim that it should be in a stretch factor group other than the lowest ranked group.

1-Staff-3s

3. Please provide API's year-over-year Achieved Regulatory Return on Equity as per RRR 2.1.5.6, for the years 2008 through 2013.

Response:

The Achieved Regulatory Return on Equity as per RRR 2.1.5.6, for the years 2008 through 2012 is:

Year	Achieved Regulatory Return on Equity
2008	7.3%
2009	6.3%
2010	5.0%
2011	10.5%
2012	11.4%
2013	6.3%

For 2008 and 2009, the Achieved Regulatory Return on Equity amount was not reported on the 2.1.5.6 as this was not a required field. The values for these years were retrieved from EB-2009-0278 Exhibit 1 Tab 2 Schedule 4 submitted June 1, 2010. For the years 2009 to 2012, the values are those originally submitted on the respective RRR 2.1.5.6 submissions.

The Achieved Regulatory Return on Equity for 2013 as per RRR 2.1.5.6 has been estimated because audited financial statements for the year ending December 31, 2013 are not finalized.

1-Staff-4s

4. Please identify other factors that the Board should consider to justify assigning a distributor like API to an alternative stretch factor group than that resulting from the benchmarking analysis.

API has prepared this report in response to this question, and also to Staff IR #2. Because our response is somewhat longer that what would typically is included in an IR response, we have organized it for the convenience of the parties into a short summary, followed by a series of sections that explain our analysis, and that in our view, justify assigning a stretch factor to API other than the one resulting from the benchmarking analysis.

Summary

Distributors are given stretch factor assignments based on their actual cost relative to costs predicted by PEG's econometric model. The PEG model predicts a distributor's costs by combining values for each distributor's output and business conditions with the coefficients (or cost drivers) developed by PEG. These coefficients have been calculated by PEG using data for all distributors, and therefore represent an averaging of all distributors.

This process has produced a value for the predicted costs for each distributor when its exact business condition variables are applied to these "average" cost drivers.

API will clearly demonstrate in this response that API is an extreme outlier within the data set used by PEG to determine its coefficients. As such, PEG's coefficients are not representative of API's own cost drivers and will produce erroneous results for API. Therefore PEG's model will understate API's predicted costs. Because the cost drivers are not representative of API's unique attributes, it is impossible for API to be assigned to any stretch factor other than the highest stretch factor on the basis of the econometric model's outcome.

The benchmarking analysis is based on five cost drivers, which include
1) the number of customers served;
2) kWh deliveries;
3) system peak capacity;
4) the average km of distribution over the sample period; and
5) the percent of customers added in the last 10 years.

Variable 4, the average km of distribution line, is intended to reflect the "business conditions" of the LDC, with respect to circumstances of the LDC's service territory and the special distribution of customers, both of which, as acknowledged by PEG based on its research, have implications for network costs.

It is the essence of API's submission that while inclusion of this variable may adequately reflect its impact on LDCs within the most typical range of values, it is not adequate to reflect the situation under which API operates and incurs its costs. The result is that the benchmarking study establishes an inappropriate efficiency standard when applied to API. API does not believe that the econometric model is reflective of API's unique attributes.

Our reasons for this conclusion are as follows:

- API is an extreme outlier in terms of customer density, as measured by number of customers per circuit km and number of customers per square km of service territory, and therefore the output of a statistical analysis of a more homogeneous population of LDCs cannot be appropriately applied to API; and
- API faces atypical factors of geography, including location on the Canadian Shield and forestation on its circuit routes, that make the efficiently incurred cost of building and maintaining its system significantly higher than that for most other Ontario LDCs, and which are not reflected in the benchmarking model.

Table 1 summarizes API's customer density in comparison with the distribution of Ontario LDCs. To prepare this table, API has used statistics compiled by the OEB in its *2012 Yearbook of Electricity Distributors*, dated August 22, 2013.

Table 1: Comparison of API's Customer Density with Ontario LDCs

	Mean of LDCs	Standard Deviation	API
Customers per Square km of Service Territory	302.79	234.46	0.82
Customers per Circuit km of Line	46.49	18.66	6.28

The following sections of this brief report, elaborate our analysis demonstrating that API is an extreme outlier in terms of customer density, and explain some of the cost incurrence issues that this business condition imposes upon API.

Cost Drivers Significant to API, Addressed in the PEG Report

In the PEG Report titled "*Productivity and Benchmarking Research in Support of Incentive Rate Setting in Ontario: Final Report to the Ontario Energy Board"* dated November 2013 (Issued on November 21, 2013 and as corrected on December 19, 2013), (the "PEG Report") PEG makes several relevant observations. Beginning on page 54 of the report, PEG states, *"Distribution cost is therefore sensitive to the circumstances of the territories in which they provide service"*, and; *"The spatial distribution of customers will therefore have implications for network costs".* Both of these statements are significant when considering the stretch factor assignment for a distributor like API, for which the spatial distribution of customers is so significantly different than for other Ontario LDCs.

At page 55 of the PEG Report, the authors elaborate on the issue:

"In addition to customer characteristics, cost can be sensitive to the physical environment of the service territory. The cost of constructing, operating and maintaining a network will depend on the terrain over which the network extends. These costs will also be influenced by weather and related factors. For example, costs will likely be higher in areas with a propensity for ice storms or other severe weather that can damage equipment and disrupt service. Operating costs will also be influenced by the type and density of vegetation in the territory, which will be at least partly correlated with precipitation and other weather variables."

In terms of the circumstances of API's service territory and the spatial distribution, API is unlike any other distributor in Ontario. This uniqueness from the perspective of spatial distribution will therefore have implications for network costs.

Table 16 of the PEG Report presents the econometric coefficients or cost drivers used for benchmarking which included the following narratives:

- Number of Customers: N = 0.4444

  A 1% increase in the number of customers raised the costs by 0.44%[1]

- Average Line Length (km): L = 0.283

  A 1% increase in the average circuit kilometers raised the costs by 0.29%[2]

- Percent of 2012 customers added in the last 10 years: NG = 0.0165

  A 1% increase in this variable increased distributor costs by 0.017%[3]

Description of API's Service Territory

API's distribution system covers an area of more than 14,200 square kilometres in a remote area of Northern Ontario, north and east of the City of Sault Ste. Marie. API serves fewer than 11,800 customers on a distribution system consisting of 1,845 kilometres of distribution line; approximately 6.3 customers per kilometer of distribution line[4]. The distribution system extends 93 km east and approximately 255 km north of the City of Sault Ste. Marie. The following map illustrates the size of API's territory, shaded in orange, relative to neighbouring LDC's denoted in blue.

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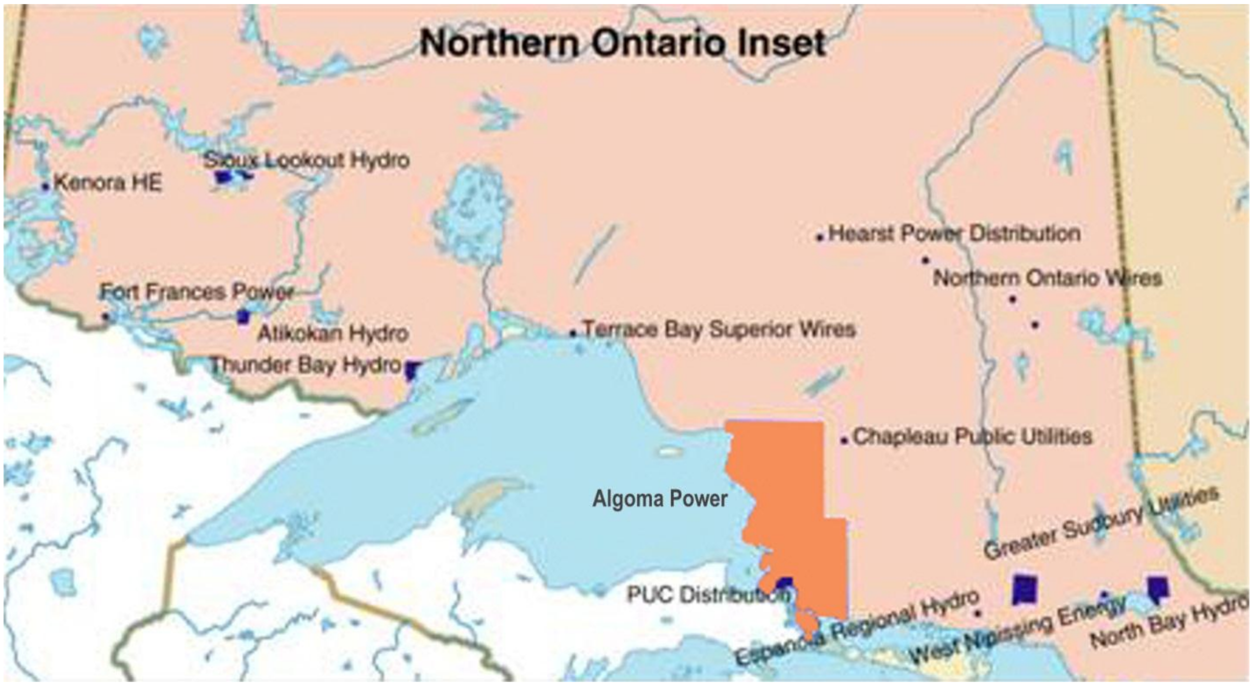
1 *The PEG Report, page 59, paragraph 2*
2 *The PEG Report, page 59, paragraph 4*
3 *The PEG Report, page 60, paragraph 2*
4 *API 2011 Cost of Service Review, EB-2009-0278, Exhibit 1 Schedule 2 Tab1, page 3*



With the exception of Hydro One Networks Inc., no other LDC in the province has a service territory as large as API's.

The low number of customers relative to its vast distribution service area, results in a very low population density within API's distribution service area. Historically, much of API's distribution system was built to service the resource sector and the communities that developed around those enterprises. As a number of those industries declined, the result was a sparsely populated service territory with predominantly residential and seasonal customers. This explains why parts of API's system are characterized by long radial lines serving very few customers.

The comments in the PEG Report that are quoted above, referring to unusual situations of geography and customer density, are therefore clearly relevant to API.

Comparison of Spatial Distribution of Customers in API and other Ontario LDCs

Using the information provided in the OEB's *2012 Yearbook of Electricity Distributors*, dated August 22, 2013, the source of data used by PEG to produce its cost drivers (coefficients), API has produced the following four charts which illustrate the distinct difference between API's service attributes and those of the general population of distributors in Ontario.

API has developed these comparisons both from the perspective of total geographical area of its service territory and the total length of line required to service its customers. In the "*Unitized Statistics and Service Auditing Requirements"* for the year ended December 31, 2012, the

Yearbook provides information related to the number of customers per square kilometer of service area and the number of customers per kilometer of line.

Figure 1 illustrates the extreme variation between API and the population of distributors used by PEG for its analysis, in terms of customers per square km of the service territory.

Figure 1

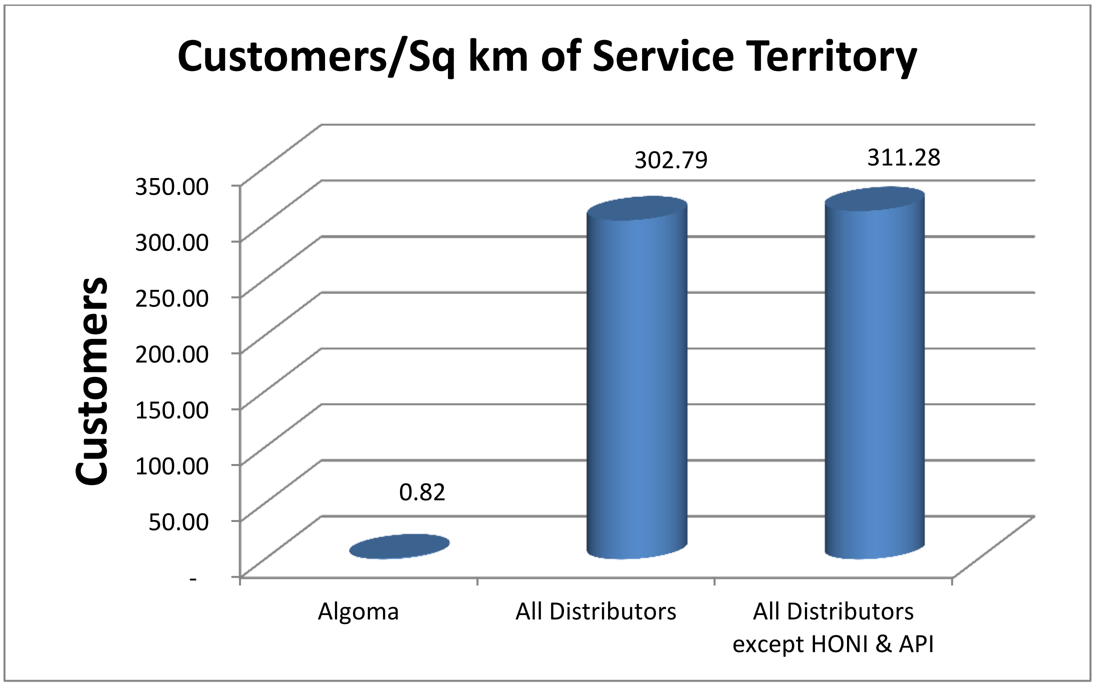
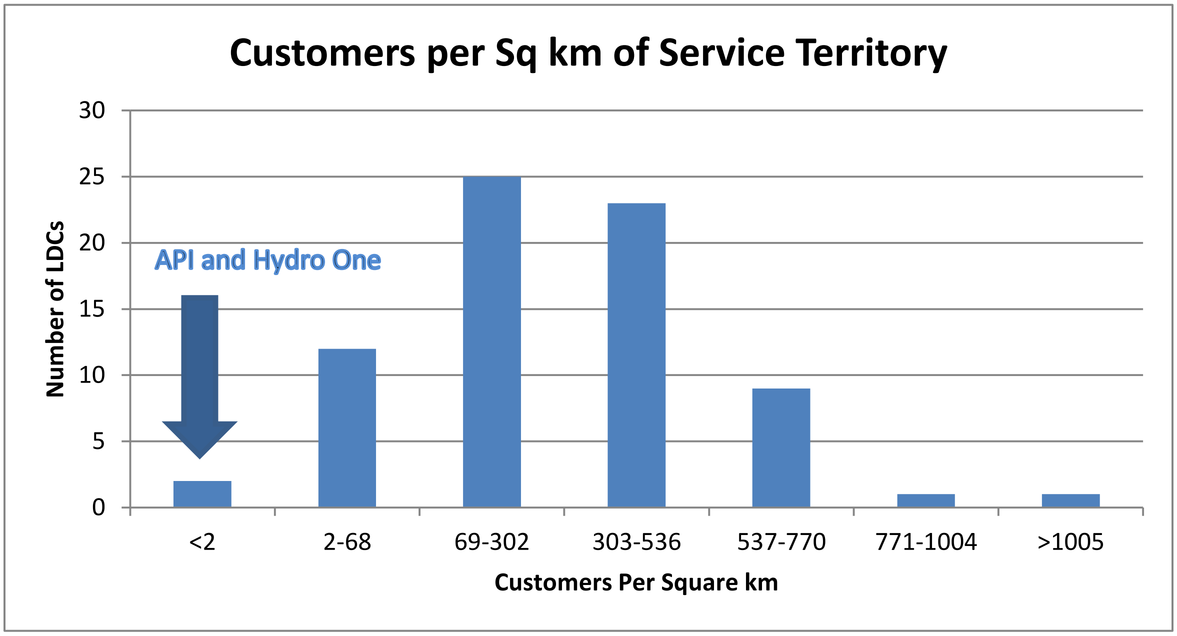


Figure 2 shows the entire population of LDCs in terms of density of customers per square km of service territory. As shown above, the mean of the distribution of 302.79, and the standard deviation is 234.46. Statistically, this indicates that approximately 68% of LDCs are expected to fall between 69 and 536 customers per square km, and in fact, 48 of the 73 LDCs are within these values. 95% of LDCs have densities between 2 and 770 customers per square km. Only Hydro One and API have densities of fewer than 2 customers per square km, and only API has a density of less than 1 customer per square km of service territory.

Figure 2



Of the twelve LDCs shown with customer densities between 2 and 68 customers per square kilometer of service territory, only two approach API and HONI with densities of approximately 5 customers per square kilometer of service territory.

Figure 3 presents a summary comparison of the density of customers per length of line of API and other LDCs. API has 6.28 customers per kilometer of distribution line while the average of all distributors, including API, is 46.49 customers per kilometer of distribution line. As shown, the variation between API and the other distributors used by PEG for its analysis is extreme.

Figure 3

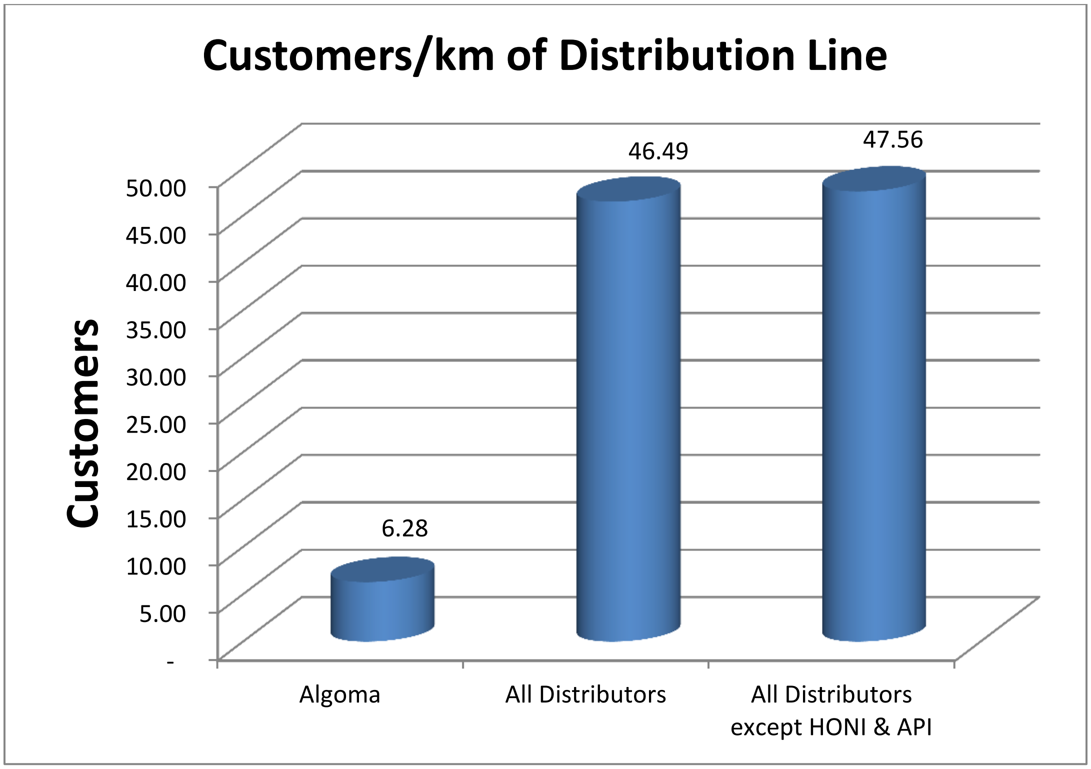
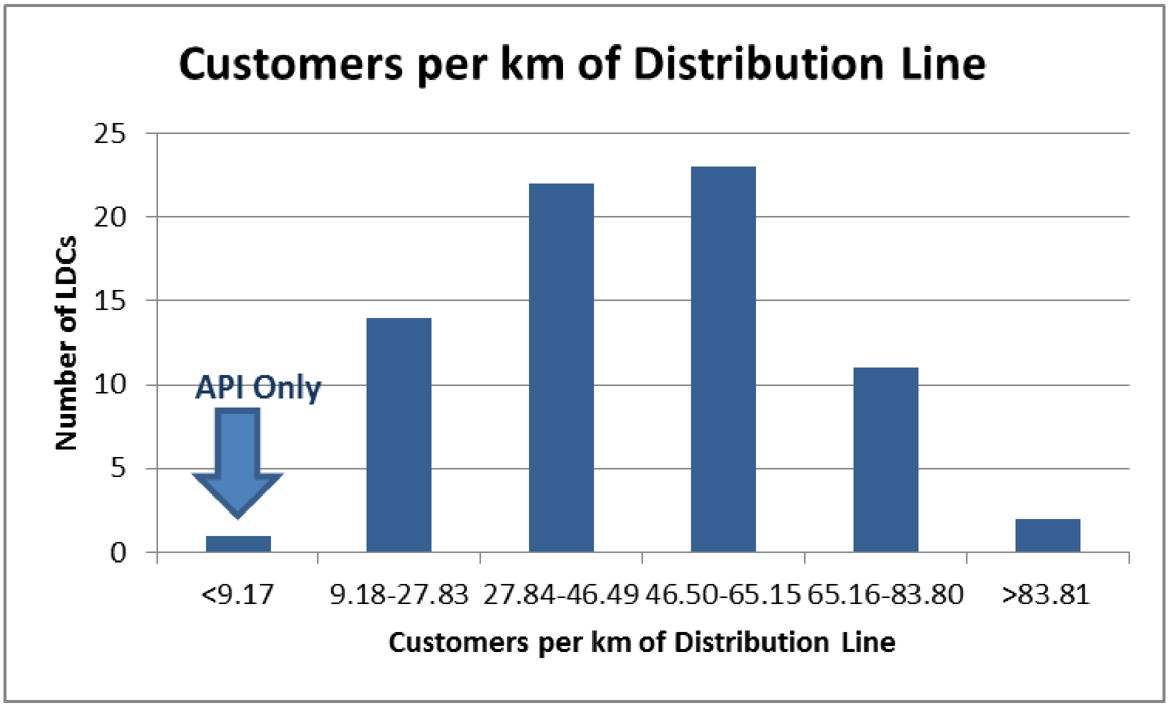


Figure 4 is a more detailed representation of the distribution of values for the variable customers per km of distribution line. The mean of the distribution is 46.49, and the standard deviation is 18.66. This means that about 68% of LDCs will fall between 27.84 and 65.15, and that 95% of LDCs will have values greater than 9.17 and less than 83.80. API is the only Ontario LDC with a number of customers per km of distribution line that is more than two standard deviations below the LDC mean.

Figure 4



Effect of Extreme Conditions of Density and Geography on Cost Incurrence in an LDC

The PEG econometric model quantifies the average expected change in cost resulting from an increase in the number of customers, an increase in the average circuit kilometers, and the percentage of customers added in the last ten years. The PEG report acknowledges that geographic conditions and distribution customer density will impact cost incurrence. The actual cost of connecting a new customer and extending the overall length of the distribution system in API's low density service territory is sensitive to these density dependant measures. Direct examples of these cost sensitivities are the extended labour costs associated with the driving time, additional fuel costs to travel longer distances and the accumulating driving distances contributing to increase vehicle maintenance cost and vehicle replacement costs.

Possibly the most evident cost associated with an increase in customers is the cost associated with distribution transformers. Distribution transformers are a prevalent and material cost for all distributors and even more so for distributors with widely dispersed low density customers as is the case with API; as shown in the Figures above, API has the lowest measure of customers per kilometer of distribution line of all distributors reported in the OEB's yearbook, and a very significantly lower measure than the average or typical LDC. With the exception of certain larger commercial and industrial customers, all customers have to be connected to a distribution transformer; the distribution transformer transforms the system voltage to the utilization voltage required by the customer.

Typically, a residential customer requires 2.5 to 5 kVA of distribution transformation capacity. Therefore, a distributor has the potential to connect 5 to 7 residential customers to a centrally located 25 kVA distribution transformer (a 25 kVA distribution transformer is the standard minimum commercially available size available).

It is common for API to have one residential customer connected to one distribution transformer; a 1:1 ratio. This means API will purchase and install a 25 kVA distribution transformer and will make all necessary line modifications associated with the transformer installation to connect one residential customer.

The OEB Yearbook does not report the information necessary to compare API's ratio of customers to installed distribution transformers. API was able to extract distribution asset information from cost of service applications filed with the Board and together with customer data from the OEB 2012 Yearbook to construct ratios for a sample of other distributors; this information is shown in Table 2. The selection of these LDCs for inclusion was strictly on the basis of availability of the data within the time permitted for response to these Interrogatories.

Table 2: Comparison of API's Customer to Distribution Transformer Ratio to other Distributors

Distributor	Customer to Distribution Transformer Ratio
Algoma Power Inc.	2.3
Canadian Niagara Power	6.2
Cornwall Electric	5.4
Burlington Hydro Inc.	8.1
Cambridge and North Dumfries Hydro Inc.	14.6
Cooperative Hydro Embrun Inc.	5.9
Hydro Hawkesbury Inc.	6.7
Oakville Hydro Electricity Distribution Inc.	9.6
Orangeville Hydro Inc.	9.2
Veridian Connections Inc.	7.0
Average Excluding API	**8.1**

This information demonstrates that the average distributor will be required to purchase, install and maintain an additional distribution transformer to support connection of eight customers;

API will have to purchase, install and maintain an additional distribution transformer to support connection of only two customers, a multiple of four. For example, if the average cost to purchase, install and maintain an additional distribution transformer is $10,000 then the average distributor will incur a marginal cost of $1,250 per customer; API's marginal cost per customer will be $5,000. This is further evidence that the PEG estimation of a 1% increase in the number of customers raising the costs by 0.44% and a 1% increase in the percent of 2012 customers added in the last 10 years increasing distributor costs by 0.017% are not valid measures on which to assess the ability of API to achieve cost efficiencies. Due to API's extremely low customer density, its cost to add additional customers will include very expensive transformer costs, costs not experienced by the general population of distributors in Ontario. These same cost drivers will be higher for API; the result of using PEG's estimated cost drivers is understating API's predicted costs.

It is therefore reasonable to extrapolate with a great degree of confidence that the coefficients presented in Table 16 of the PEG report and set out earlier in this response are not valid in API's circumstance and therefore unreliable as cost drivers to predict costs for API, and therefore also inappropriate to use as a standard to measure the level of cost efficiency that API should be able to achieve.

Geography and Low Density Drive High Investment in Property, Plant and Equipment per Customer

A further clear indicator of API being an extreme outlier is the measure of property plant and equipment that must be supported and maintained in order to provide service in its vast service territory. The OEB's *2012 Yearbook of Electricity Distributors*, dated August 22, 2013, indicates that the total gross property plant and equipment for API was $137 million or $11,285 per customer. Figure 5 below compares total property plant and equipment per customer for API to the average for Ontario distributors.

The reason for the high amount of plant investment per customer in API is the length of distribution line that is installed, on average, per customer, as well, as discussed previously, as a correspondingly high base of assets such as transformers. The longer distances create a requirement for more vehicles and equipment per customer in order to build, operate and maintain the system.

Figure 5

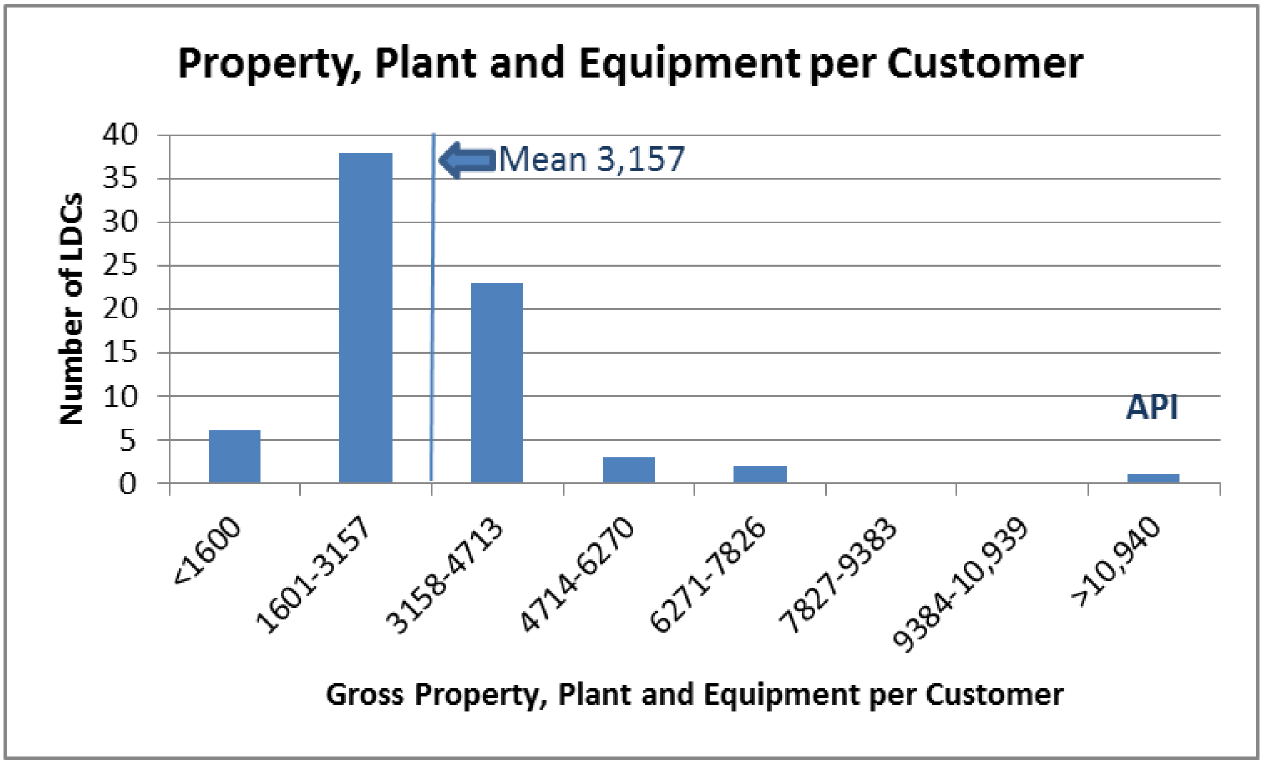


Figure 5 reflects the distribution of gross property, plant and equipment per customer in the population of Ontario LDCs, Frequency distribution "bins" shown in the graph are defined by the mean of the population, which is $3,157 per customer, and the standard deviation of the distribution, which is $1,557. With $11,285 in gross property, plant and equipment per customer to operate and maintain, API is more than five standard deviations from the average of Ontario LDCs. On the basis of property, plant and equipment per customer, Ontario LDCs are relatively homogeneous, with 83% (61 of 73) falling within one standard deviation of the mean.

It is relevant to note that if API is excluded from the population, the mean property, plant and equipment per customer for Ontario LDCs is reduced to $3,036, and the standard deviation is greatly reduced (from $1,557 to $1,182).

Effect of Forestry on Costs

While Ontario's beautiful trees present a challenge and a cost even in the densely populated areas of the GTA, nowhere are the challenges and the costs as significant as in rural northern

Ontario, and most specifically for API, where the length of distribution line per customer is so high.

Vegetation management costs are a significant cost driver for API. In its last cost of service review, API presented a test year budget of $2.5 million for vegetation management; approximately $2,100 per customer. API's service territory is geographically vast and heavily forested; other than Hydro One, it has no comparator in Ontario. API's distribution facilities are primarily located on crown land and/or corporately controlled land tracks. These land control authorities, including the MNR, are introducing new fees to API making its vegetation management cost more than otherwise forecasted. These fees include both stumpage fees and licence/permitting fees; all of which are volumetric based.

The photograph shown below is indicative of the terrain that API's distribution lines traverse and the vegetation management required to maintain a safe and reliable distribution system.

These increasing costs of establishing and maintaining this type of right-of-way, embedded within the API OM&A accounts, are not commonly associated with other distributors in the PEG sample group and therefore not adequately weighted in PEG's cost drivers.

1-Staff-5s

5. The Board has approved inflation and productivity factors of 1.7% and 0% respectively, for 2014 rates. As well, the Board has approved a range of stretch factors. Please complete the following chart reflecting API's estimated impact for 2014 for each of the stretch factors below.

Board-Approved Stretch Factors					
	0.0%	0.15%	0.30%	0.45%	0.60%
Estimated 2014 Revenue Collected through Rates Adjusted by Stretch Factor					

Response:

In the table provided below, API has estimated the impact to the 2014 revenue to collected through rates for each of the stretch factors. The basis of the revenue collected through rates is the total revenue requirement approved by the Board in API's 2013 incentive rates application, EB-2012-0104. The effective revenue requirement arising from that proceeding was $20,079,236.

Board-Approved Stretch Factors					
	0.0%	0.15%	0.30%	0.45%	0.60%
Estimated 2014 Revenue Collected through Rates Adjusted by Stretch Factor	$20,420,583	$20,390,464	$20,360,345	$20,330,226	$20,300,108
Incremental Impact	Nil	$30,119	$60,238	$90,357	$120,475

This interrogatory asked for revenue collected from rates. However, it is important to note that the manner in which incentive regulation is applied in Algoma (i.e., the methodology accepted in API's first incentive based application: EB-2011-0152 and EB-2012-0104). The accepted methodology recognizes the interconnection of revenue derived from distribution rates, the RRRP funding amount and the utilization of the equivalent distribution rates. With this accepted methodology, it is impossible to segregate RRRP funding from revenue from distribution as the two are intertwined by the respective implementations of the RRRP-Adjustment Factor and the Price Cap Index.

1-Staff-6s

6. As stated in the Report of the Board on Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's approach to assigning stretch factors to distributors is based on a distributor's actual costs relative to its predicted costs as estimated by benchmarking analysis. The approach does not compare one distributor to another distributor. In its supplementary evidence, API states that the PEG econometric model does not accurately assess and compare the efficiency of API within the general operating environment of distributors in Ontario.
   a. Please explain why the benchmarking analysis should not apply to API, including reasons supporting API's statement in the preamble above.
   b. Is it API's view that it can no longer incorporate efficiencies to lower distribution costs? If so, please explain.

Response:

a. API agrees that the approach to assigning stretch factors to distributors is based on a distributor's actual costs relative to its predicted costs as estimated by benchmarking analysis. The issue lies in the coefficients (or cost drivers) used in the model which is predicting the costs for API.

   The coefficients used to construct this estimation model have been developed using the industry as a whole and therefore are reflective of the general population of Ontario distributors. Individual distributor costs were predicted by inserting values for each distributor's output and business condition variables into a cost model that is "fitted" with the coefficients presented in Table 16[1].

   API asserts that a model which uses the metrics developed for a population of distributors that do not share the same geographical and cost attributes as does API will not appropriately predict API's costs because API's particular attributes will give rise to materially different coefficients.

b. No, it is not API's view that it can no longer incorporate efficiencies to lower distribution costs. API has expressed the view that as a high cost lower revenue distributor it may not have been appropriately characterized in the assignment of stretch factors. API accepts and acknowledges the importance of the stretch factor. API believes that it be may be more appropriate, given its uniqueness, to assess future efficiencies and inefficiencies against its own actual costs. Should API be able to reduce its controllable costs on a go forward basis then the onus ought to be on API to present evidence as to why its stretch factor should be decreased from a starting point. Likewise, if these same costs increase than the onus should be on API to present evidence as to why its stretch

[1] PEG Report, page 61, paragraph 1

factor ought not to be raised. API's annual scorecard will provide sufficient information to inform the Board.

API believes the starting point should be a stretch factor of 0.3%, the midpoint.

1-Staff-7s

7. Board staff notes that the manner in which the RRRP mechanism has been established guarantees API a substantial portion of its revenue requirement because it is not load dependent. For 2014 rates, this portion will likely be more than 50%. All things being equal, this reduces business risk. In the Board's Decision and Order related to Algoma's 2012 IRM application (EB-2011-0152), the Board noted that:

   "To award a stretch factor that is different from that set out in the letter would have the effect of providing incremental relief to the utility for those qualities that are already appropriately dealt with via the RRRP mechanism."

   Please explain why the benefits associated with a reduction in business risk are not sufficient to address or offset API's high costs (as a result of its low density, low revenue profile).

Response:

We assume that Board staff is suggesting that the RRRP mechanism guarantees that API will **collect** a substantial portion of its revenue requirement. As the interrogatory is written, it could be interpreted to suggest that Board staff believes that the **approval** of substantial portion of API's revenue requirement is guaranteed by the RRRP mechanism. This would be incorrect, since even with the RRRP mechanism the Board still has to approve API's proposed revenue requirement, subject to the same evidentiary standards and scrutiny as any other LDC. API has no guarantee of revenue requirement approval, as subsection 3.1 of the RRRP regulation provides "as approved by the Board" in reference to forecast revenue requirement.

Based on the assumption described above, Board staff seems to be asking whether the benefit of reduced business risk resulting from the RRRP mechanism would offset the detriment of using a standard stretch factor assignment for API (i.e. resulting in a fair outcome for API).

There are a number of issues that API wishes to address as part of its response to this interrogatory:

1) There is no interaction between reduced risk of collecting revenue resulting from the RRRP mechanism and API's stretch factor. The "interaction" that API interprets Board staff to be pursuing is the neutralization of a benefit (reduced collection risk) by using what API believes to be an inappropriate stretch factor to even the playing field for API. This is not an interaction between the RRRP subsidy and the metrics used to assess API's efficiency category. It is artificial justification for disputing the stretch factor proposed by API.

Technically, the return on equity ("ROE") built into API's rates is set by the Board's ROE formula which includes a risk premium. By using the benefit of a reduced risk of collecting revenue to justify an inappropriate stretch factor for API, Board staff is suggesting that the Board's ROE formula does not work in API's case. API does not believe that it is appropriate for Board staff to attempt to indirectly adjust API's ROE through the stretch factor. API's ROE was approved by the Board in its last cost of service rate application. Further, the Board does not adjust distributors' ROE during the IRM period. Finally, the ROE formula is applied generically to all distributors and is not subject to adjustment (either directly or indirectly) in this proceeding.

2) In the absence of a clear definition of the term business risk, it is impractical for API to associate a monetary measure with it. On the other hand, for Board staff to suggest "a reduction in business risk" may in some manner equate to an arbitrary assignment of a stretch factor for API is measurable. As provided earlier in the response to Interrogatory No. 5, each increment in the stretch factor equates to a revenue change of $30,199. Therefore, assigning a stretch factor of 0.6% to API as opposed to 0.3% believing it is justified because of a perceived reduction in business risk arising from the RRRP will cost API $60,238 annually. Because API is unable to associate a monetary measure to reduced "business risk", we are unable to comment on whether quantitatively the value of the benefit of reduced business risk would set off the value of the detriment ($60,238 annually) of using an inappropriate stretch factor assignment for API. In any event, for the reasons set out in #1 above, API does not believe that a set-off in this circumstance is appropriate.

3) Board staff has asked API to explain "why the benefits associated with a reduction in business risk are not sufficient to address or offset API's high costs (as a result of its low density, low revenue profile)." By doing so, Board staff has placed the onus on API to refute Board staff's presumption that the benefits associated with a reduction in business risk are sufficient to address or offset API's high costs. It is unfair and unreasonable for Board staff to make an unsubstantiated assertion and expect API to refute it.

In conclusion, API believes there is no interaction between API's eligibility for the Rural and Remote Rate Protection subsidy and the metrics used to assess API's efficiency category.