January 29, 2014

Kirsten Walli, Board Secretary
Ontario Energy Board
P.O. Box 2319, 27th Floor
2300 Yonge Street
Toronto, ON
M4P 1E4

Attention: Ms. Walli

Re: Espanola Regional Hydro Distribution Corporation's ("ERHDC") 2014 IRM Rate Application
Reply Submission
Board File No. EB-2013-0127

In accordance with Procedural Order No. 1 dated November 22, 2013, please find attached ERHDC's reply submission in the above proceeding.

ERHDC has filed these responses pursuant to the Board's e-Filing Services and two hard copies of the responses will be delivered to the Ontario Energy Board.

In the event of any additional information, questions or concerns, please contact Jennifer Uchmanowicz, Rate and Regulatory Affairs Officer, phone number: (705) 759-3009 or email: Jennifer.Uchmanowicz@ssmpuc.com.

Sincerely,

Jennifer Uchmanowicz

_____

Jennifer Uchmanowicz
on behalf of Espanola Regional Hydro Distribution Corporation
Rates and Regulatory Affairs Officer
PUC Services Inc.
Sault Ste. Marie Ont.
Email: Jennifer.Uchmanowicz@ssmpuc.com
Phone: 705-759-3009

Reply Submission
Espanola Regional Hydro Distribution Corporation
2014 IRM Rate Application
EB-2013-0127

Introduction

Espanola Regional Hydro Distribution Corporation ("ERHDC") filed an application (the "Application") with the Ontario Energy Board (the "Board") on October 18, 2013, seeking approval for changes to the distribution rates that ERHDC charges for electricity distribution to be effective May 1, 2014. The Application is based on the 2014 Incentive Regulation Mechanism ("IRM"). ERHDC respectfully submits this document as a reply submission to the Board.

RTSR Workform

Issue

ERHDC completed the RTSR Workform and Board staff had no concerns with the data supporting the updated Retail Transmission Service Rates proposed by ERHDC.

On January 9, 2013 the Board issued its Rate Order for Hydro One Transmission (EB- 2012-0031) which adjusted the UTRs effective January 1, 2014, as shown in the following table:

2014 Uniform Transmission Rates

Network Service Rate	$3.82 per kW
Connection Service Rates	
Line Connection Service Rate	$0.82 per kW
Transformation Connection Service Rate	$1.98 per kW

Board staff indicated it will update ERHDC's RTSR Workform at the time of the Decision in this proceeding.

ERHDC Comments

ERHDC has no further comments on this issue and is in agreement with the Board staff's submission.

Deferral and Variance Account Disposition

Issue

ERHDC's total Group 1 Deferral and Variance Account balances amount to a credit of $145,045. The balance of Account 1589 – Global Adjustment is a debit of $151,308, and is applicable only to Non-RPP customers. These balances also include interest calculated to April 30, 2014. Based on the threshold test calculation, the Group 1 Deferral and Variance Account balances equate to

$0.0023 per kWh which exceeds the threshold, and as such, ERHDC requested disposition of these Accounts over a two-year period. Board staff reviewed ERHDC's Group 1 Deferral and Variance Account balances and noted that the principal balances as of December 31, 2012 reconcile with the balances reported by ERHDC pursuant to the *Reporting and Record-Keeping Requirements*. Also, the pre-set disposition threshold has been exceeded. Accordingly, Board staff has no issue with ERHDC's request to dispose of its 2012 Deferral and Variance Account balances at this time over the requested two-year period.

ERHDC Comments

ERHDC has no further comments on this issue and is in agreement with the Board staff's submission.

Incremental Capital Module ("ICM")

Introduction

ERHDC proposed to recover, through an ICM, the incremental capital costs of $2,062,500 associated with the construction of a new municipal substation plus a required 44kV line. ERHDC proposed to allocate the revenue requirement associated with the incremental capital expenditures eligible for cost recovery ($168,193) on the basis of distribution revenue. ERHDC proposed to recover these amounts by means of fixed and variable rate riders with a sunset date of April 30, 2017. ERHDC is scheduled to file its next rebasing application for 2016 rates. The *Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors* requires that incremental capital expenditures satisfy the eligibility criteria of materiality, need and prudence in order to be considered for recovery prior to rebasing. To qualify for an ICM, applicants must demonstrate that amounts exceed the Board-defined materiality threshold; clearly have a significant influence on the operation of the distributor; must clearly be non-discretionary; and the amounts must be outside the base upon which rates were derived.

Issue - Materiality

Board staff notes that EHRDC filed its ICM workform with a default price cap index of 0.58%. On November 21, 2013 the Board issued its Report (EB-2010-0379) *Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors* ("Price Cap IR Report"). Accordingly, the inflation factor for 2014 rates is 1.7%. Based on the total cost benchmarking model developed by Pacific Economics Group Research LLC, the Board determined that the appropriate value for the productivity factor is zero percent. The Board also determined that the stretch factor can range from 0.0% to 0.6% for distributors selecting the Price Cap IR option and is assigned based on a distributor's cost evaluation ranking. In the Price Cap IR Report, the Board assigned ERHDC a stretch factor of 0.15%. The resulting price cap index is 1.55% (1.70% - 0.15%).

Based on this updated price cap index, Board staff calculated the revised materiality threshold to be $335,084. The revised amount eligible for incremental capital funding would then be

$2,080,779 (the total non-discretionary capital budget of $2,415,863 less the revised materiality threshold of $335,084). Board staff submits the requested amount of $2,062,500 for the new substation and 44kV line is clearly above the materiality threshold and within the amount eligible for incremental funding. VECC also submits the incremental capital requested by Espanola ($2,062,500) is eligible for ICM treatment as it exceeds the materiality threshold.

ERHDC Comments

ERHDC has no further comments on this issue and is in agreement with the Board staff and VECC's submission that the requested amount of $2,062,500 for the new municipal substation and the 44 kV line build is clearly above the materiality threshold. ERHDC has included with this reply submission an updated ICM workform with the revised price cap index of 1.55% (Espanola_ReplySUB_Incremental Capital Wrkfrm_20140129).

Issue - Project Need and Prudence

ERHDC indicated that the incremental capital expenditures are related to the construction of a new municipal substation scheduled to be in-service by the fall of 2014. The new substation and 44 kV line are being constructed to provide additional capacity as well as act as a contingency for ERHDC's three other substations. ERHDC stated that the new substation is critical to ERHDC's infrastructure. ERHDC provided evidence that the present capacity matches almost exactly the winter loading requirements with no contingency for failure or maintenance by the remaining stations. ERHDC addressed the need for the new substation in its 2012 Cost of Service rate application indicating planning and construction was on the horizon. Espanola indicated at that time that it intended to utilize the ICM to address the treatment of new capital needs. ERHDC stated that a Condition Assessment Study performed in 2008 indicated that all three of the existing substations are approaching the end of their useful life. A Substation Contingency Report prepared in 2010 by Costello Associates indicated that winter-time failure would most likely result in prolonged lengthy outages and rotating blackouts lasting several days. In addition to adding capacity, ERHDC noted that the new municipal substation will be compatible with any level of automation or SCADA.

In October 2013, ERHDC retained the services of Costello & Associates to provide advice on the technical details of the new substation. A Municipal Substation Report ("2013 Report") was prepared. The 2013 Report concluded that ERHDC should design and construct a new municipal substation to provide additional capacity for system growth as well as providing the necessary system security for an unplanned station failure at one of the existing substation. The 2013 Report stated it is consistent with current Ontario LDC planning practices.

ERHDC provided an evaluation of the following alternatives as part of the 2013 Report:

1. Expand the existing station – Stations MS-1 and MS-2 at 5000kVA are at maximum design capacity for 4 kV, while MS-3, rated 3000kVA could increase its capacity to 5000kVA.
2. Purchase Spare Transformer – ERHDC could purchase and store a spare transformer to

be used as an emergency replacement in the event of failure at one of the existing station transformers.

3. New Substation - Build a new 5000kVA substation in the south-west area of Espanola including land acquisition and building of a 44kV supply line. Three possible scenarios for doing so are set out below:
    a. Install a new substation with the same design as the existing station ($1.45M).
    b. Construction of a substation building, housing indoor metalclad switchgear, stand-alone protection and control rack and a SCADA/P&C/Communication rack ($2.75M).
    c. Install Outdoor 44kV Padmounted Switchgear, Underground Construction Padmounted Reclosers and isolating Switches, Underground 4.16KV Risers x 3 ($1.78M).
4. Do Nothing

Based on the recommendation by Costello and Associates, ERHDC selected option 3c, the construction of a new substation and the build of the required 44kV line to provide additional capacity and increase supply security.

ERHDC stated that a failure to approve the incremental capital rate riders would have short-term financial implications for ERHDC. ERHDC stated that it would have to evaluate the progress of the construction, which might need to be halted until ERHDC would be eligible to re-base in 2016. ERHDC further stated that without the ICM rate rider, it would experience difficulty meeting the obligations of an Infrastructure Ontario loan, which was secured for this project as well as experiencing some short-term financial implications.

In Board staff's submission it requested that ERHDC confirm the estimate for option 3c includes protection and control and a SCADA/P&C/Communication rack in exhibit 12 of the application.

Board staff noted that ERHDC did not provide a cost estimate/business case for option one and two. Board staff submits ERHDC should provide a cost comparison between the various options, including the 'Do nothing' option. Otherwise, Board staff submitted it takes no issue with the design of the substation selected by ERHDC.

VECC noted in its submission a cost estimate is not provided for the alternative to purchase a spare transformer (option 2). VECC asked that Espanola provide a cost estimate in its reply submission. VECC noted due to design complexities this option has the potential for unplanned outages and rolling blackouts which is inconsistent with the project objective to have immediate backup station capacity in the event of a failure of one of the existing substations. The risk of unplanned outage and the resulting impact on customers makes this option undesirable.

VECC submits that Espanola has provided substantive evidence in the past and in the current application to support the need to provide additional capacity on its system should one of its existing municipal substations fail under moderate to heavy load conditions. VECC submitted that it agrees based on the evidence provided that the alternative to expand or rebuild one or more of the existing stations is not feasible and submits this alternative does not adequately address Espanola's capacity shortage issue.

With respect to building a new station, VECC submits that although Espanola's preferred alternative (the new substation at a cost of $1,787,500) is not the least initial cost for rate payers, it represents the most cost-effective option for ratepayers. In VECC's view constructing a new substation based on old technology is inconsistent with current Ontario LDC practices and does not make sense. Neither does a design that costs more but does not provide any significant operational benefits over the preferred option.

VECC submits Espanola's ICM request meets the Board's eligibility criteria with respect to materiality, need and prudence.

With respect to the need and timing, Board staff submitted it has no concerns subject to confirmation that the new substation will be used and useful in 2014. VECC stated in its submission that providing the new substation is in-service in 2014, VECC takes no issue with Espanola's ICM request.

ERHDC Comments

ERHDC confirms, as per Board staff's request, that the estimate for option 3c (building a new substation) includes modern protection, control and SCADA functionality.

Requested Cost Estimates

Option 1 relates to expanding or rebuilding one of the existing substations. Substation MS-1 and MS-2 are rated 5,000 kV each and are at the maximum design capacity for a 4kV system. The MS-3 station is rated 3,000kV and its capacity could be increased to 5,000kV. This option does not provide sufficient incremental capacity to supply the Town in the event of a failure of MS-1 or MS-2. It would require a lengthy outage during construction at which time the remaining 2 stations could not handle the peak town load. This option is not a feasible alternative. The cost estimate for this option is at $800,000.

Option 2 relates to purchasing a spare transformer to use as an emergency replacement in the event of a failure of an existing station transformer. Due to the different configurations of the existing substations, it would be difficult to have a spare transformer that would easily be installed in all of the substations. This option is not feasible and could result in lengthy unplanned outages and rolling blackouts. The estimated cost for purchasing a spare

transformer, temporary primary and secondary cables, plus allowance for emergency framing and connection to the overhead systems is estimated to be $275,000.

Option 4 which is the "do nothing alternative" has 2 possible impacts. Firstly, in the event of a failure of one of the existing substations, there could be prolonged power outages. This likely would result in rotating blackouts or long-duration outages until such time a replacement transformer or other major components could be sourced, purchased, delivered and installed. Secondly, there is not a significant amount of spare capacity available for any planned load growth and this may result in an adverse impact on economic development opportunities. Doing nothing is not a feasible option. The cost estimate of a failure of an existing substation depends on which component has failed; therefore ERHDC has not provided a cost estimate for this option as the costs can vary significantly.

ERHDC confirms the new municipal substation is planned to be in-service in 2014.

ERHDC has no further comments on this issue and agrees with VECC and Board Staff that the ICM request meets the Board's eligibility criteria with respect to materiality, need and prudence.

Issue - The Incremental Revenue Requirement Calculation

The Board's general guidance on the application of the half-year rule is provided in the *Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors* dated September 17, 2008. In this report the Board determined that the half-year rule should not apply so as not to build a deficiency for the subsequent years of the IRM plan term. Since ERHDC is scheduled to be rebased in 2016, Board staff submits that ERHDC correctly did not apply the half-year year.

Board staff submits that the capital structure and the cost of capital parameters used are consistent with *Chapter 3 of the Filing Requirements for Electricity Distribution Rate Applications*, dated July 17, 2013 ("the Filing Requirements").

Board staff submits that the revenue requirement calculation of $168,193 provided by ERHDC is consistent with the Filing Requirements.

ERHDC Comments

ERHDC has no further comments on this issue and is in agreement with the Board staff's submission.

Issue - Recovery of the Incremental Revenue Requirement

ERHDC proposed to allocate the revenue requirement associated with the incremental capital expenditures eligible for cost recovery ($168,193) on the basis of a combination of fixed and variable rate riders. In response to Board staff interrogatory #6b, ERHDC confirmed that the proposed fixed/variable split is consistent with the split used to calculate ERHDC's current

Board-approved distribution rates.

In the application, ERHDC requested a sunset date of April 30, 2017 and noted that it expects to file a Cost of Service application for the 2017 rate year. In response to Board staff interrogatory #2, ERHDC confirmed that its current IRM plan term is 4 years and that it is scheduled to rebase in 2016. ERHDC agreed to forgo a defined sunset date and establish a rate rider that would be effective until the next cost of service-based rate order.

Board staff submits it is of the view that a variable rate rider is administratively more straightforward than the additional complexities of rider with fixed and variable components. The stability of energy consumption levels by ERHDC would present little risk to recovering the ICM revenue amounts.

VECC submitted that foregoing a sunset date and establishing a rate rider that would be effective until its next cost of service rate order is an appropriate approach.

ERHDC Comments

ERHDC agrees to forego a sunset date for the ICM rate rider and establish rate riders that would be effective until its next cost of service rate order. Espanola agrees the ICM rate rider will not have a fixed component due to the additional complexities with a variable and fixed ICM rate rider.

Lost Revenue Adjustment Mechanism for Pre-2011 CDM Activities

Issue

Section 13.6 of the Board's *Guidelines for Electricity Distributor Conservation and Demand Management* (the "CDM Guidelines") issued on April 26, 2012 outlines the information that is required when filing an application to recover LRAM amounts related to pre-CDM Code or pre-2011 CDM Activities.

In ERHDC's 2012 Cost of Service rate application (EB-2011-0319) the Board approved an LRAM amount of $152,728, related to CDM programs implemented from 2006 to 2010 for the period 2006 to 2010. The Board did not approve the recovery of lost revenue due to the persistence from 2006 to 2010 programs in 2011 and 2012 ($7,544) as it was considered premature to do so and inconsistent with the LRAM Guidelines.

In the application, ERHDC is seeking recovery of an LRAM amount of $7,544 related to persisting CDM savings from pre-2011 programs in 2011 and the first four months of 2012 until April 30, 2012 when Espanola rebased.

VECC submitted that ERHDC is eligible for its proposed LRAM recovery of $7,544 related to pre-2010 programs in 2011 until April 30, 2012 as these saving occurred prior to the updated load forecast established in Espanola's 2012 Cost of Service Rate application.

In its submission, Board staff supported the recovery of the LRAM amount of $160,270 as Espanola was either under IRM during the years related to its request or did not otherwise have an opportunity to recover the lost revenues.

ERHDC Comments

In ERHDC's 2012 Cost of Service Rate application (EB-2011-0319) an LRAM amount of $152,728 was approved for recovery which represents the effect of CDM programs implemented from 2006 to 2010 for the period 2006 to 2010. It should be noted that in this application ERHDC is applying for the persisting losses from pre-2011 programs in 2011 until April 30, 2012 of $7,544 not the entire LRAM amount of $160,270. ERHDC has no further comments on this issue and is in agreement with the LRAM recovery of $7,544.

- All of which is respectfully submitted -