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BY EMAIL

February 3, 2010

Ontario Energy Board
P.O. Box 2319
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2300 Yonge Street
Toronto ON M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

**Re: Board Staff Submission on Welland Hydro-Electric System Corp.
2010 Electricity Distribution Rates Application
Board File Number EB-2009-0252**

Please see attached Board staff's submission for the above proceeding. Please forward the attached to Welland Hydro-Electric System Corp. and any intervenors in this proceeding.

Welland Hydro-Electric System Corp.'s reply to submissions is due February 24, 2010.

Yours truly,

Martin Benum
Advisor, Applications and Regulatory Audit



ONTARIO ENERGY BOARD

STAFF SUBMISSION

2010 ELECTRICITY DISTRIBUTION RATES

Welland Hydro-Electric System Corp.

EB-2009-0252

February 3, 2010

**Board Staff Submission
Welland Hydro-Electric System Corp.
2010 IRM3 Rate Application
EB-2009-0252**

Introduction

Welland Hydro-Electric System Corp. ("Welland") filed an application with the Ontario Energy Board (the "Board"), received on October 20, 2009, under section 78 of the Ontario Energy Board Act, 1998, seeking approval for changes to the distribution rates that Welland charges for electricity distribution, to be effective May 1, 2010. The application is based on the 2010 3rd Generation Incentive Regulation Mechanism.

The purpose of this document is to provide the Board with the submissions of Board staff based on its review of the evidence submitted by Welland.

Board staff makes submissions on the following matters:

- Potential Tax Sharing Rate Rider;
- Disposition of Deferral and Variance Accounts as per the Electricity Distributors' Deferral and Variance Account Review Report (the "EDDVAR Report");
- Treatment of Smart Meter Funding Adder;
- Adjustments to the Revenue to Cost Ratios;
- Adjustments to the Retail Transmission Service Rates; and
- Accounting for the implementation of the Harmonized Sales Tax ("HST").

POTENTIAL TAX SHARING RATE RIDER

General Background

The Supplemental Report of the Board on 3rd generation incentive regulation issued on September 17, 2008 determined that a 50/50 sharing of the impact of currently known legislated tax changes, as applied to the tax level reflected in the Board-approved base

rates for a distributor, is appropriate. The calculated annual tax changes over the plan term are to be allocated to customer rate classes on the basis of the Board-approved base-year distribution revenue. These amounts will be collected from or refunded to customers each year of the plan term, over a 12-month period, through an explicit volumetric rate rider derived using annualized consumption by customer class underlying the Board-approved base rates.

Welland Specific Background

Using the Board's Supplemental Filing module Welland's Tax Sharing amount is a refund of \$18,110. This amount when unitized using Welland's volumetric billing determinants results in energy-based kWh rate riders less than four decimal places and demand-based kW rate riders less than two decimal places.

Submission

Board staff notes that as a result of having kWh Tax Sharing rate adders of \$(0.0000) when rounded to the fourth decimal place and kW Tax Sharing rate adders of \$(0.00) when rounded to the second decimal place, the refund amount of \$18,110 will not be returned to ratepayers, which defeats the intent of tax sharing process. Board staff submits that the Board may wish to consider directing Welland to record the Tax Sharing refund amount of \$18,110 in the variance account 1595 for disposition in a future rate setting.

DISPOSITION OF DEFERRAL AND VARIANCE ACCOUNTS AS PER THE EDDVAR REPORT

General Background

For purposes of 2010 IRM applications, the EDDVAR Report requires a distributor to determine the value of its December 31, 2008 Group 1 Deferral and Variance account balance and determine whether the balance exceeded the preset disposition threshold

of \$0.001 per kWh using the 2008 annual kWh consumption reported to the Board. When the preset disposition threshold is exceeded, a distributor is required to file a proposal for the disposition of Group 1 account balances (including carrying charges) and include the associated rate riders in its 2010 IRM Rate Generator for the disposition of the balances in these accounts. The onus is on the distributor to justify why any account balance in excess of the threshold should not be cleared.

Any distributor exceeding the preset disposition threshold was required to file a Deferral and Variance Account Workform.

Welland Specific Background

Annual Disposition

Welland has requested the disposition of its Group 1 account balance. Board staff interrogatory #5a requested that Welland complete and submit an updated version 4 of the Deferral Variance Account Workform. Welland has complied with this request.

Global Adjustment

In response to Board staff interrogatory # 1a, Welland stated it had reviewed the Regulatory Audit & Accounting Bulletin 200901 and confirmed that it had accounted for its Account 1588 RSVA power and global adjustment sub-account in accordance with this Bulletin.

In response to Board staff interrogatory #1b, Welland confirmed that it did make adjustments subsequent to its initial application to comply with the Regulatory Audit & Accounting Bulletin 200901 with respect to account 1588 and the global adjustment sub-account. However Welland noted that it "was not accounting properly for the monthly adjustment between revenue or cost of power (was only adjusting revenue). In addition, regulatory interest expense had been taken against interest income. However,

these are just presentation issues which do not reflect in the balances of the variance accounts.”

In response to Board staff interrogatory #2a, Welland disagreed that a separate rate rider be prospectively applied to non-RPP customers to dispose of the global adjustment sub-account balance would be appropriate on the basis of cost causality. Welland noted:

“The Provincial Benefit charge is set on a monthly basis. The RPP rates are set every six months. Welland Hydro's Customer Service Representatives spend a significant amount of time explaining to Residential Retailer customers what the Provincial Benefit charge is for and why it has increased so significantly over time. These customers are advised that the RPP rates include an amount for the Provincial Benefit. However, as the RPP rates are only set twice per year it is unclear if the Provincial Benefit portion is based on a retrospective or prospective basis and whether any true up occurs.

Welland Hydro did not clear the 1588-Global Adjustment as part of the 2009 Rate Application. As a result, this balance represents the variance since the inception of the Global Adjustment charge. As a result, it would be unfair to charge these variances to customers who have recently switched from RPP to Non-RPP.

Billing determinants for GS>50kW, Large Use, Sentinel Lights, and Street Lights are based on kW. For customers with a high demand there are significant variations in the correlation between kW and kWh which is used to bill the Provincial Benefit charge. A plant operating on a one shift basis at a 5,000 kW peak demand would pay the same global adjustment rate rider as a plant operating on a three shift basis at the same peak demand yet consuming far more kWh. Perhaps a more appropriate basis to apply the 1588-Global

Adjustment rate rider to Non-RPP customers would be on kWh which reflects the basis on how the variance was created.”

In response to Board staff interrogatories #2b, Welland stated that it did currently have the billing capability to have a separate rate rider applicable to non-RPP customers to dispose of the global adjustment sub-account balance. Welland however noted that its “billing system can handle such a rate rider but there are questions in regards to its use. The first question is would this rate rider be a separate line item on the bill or included with distribution charges? The use of a separate line item would lead to significant questions from Residential Retailer customers. The second point would be to ensure that the billing system used billing determinants before line losses. The current Provincial Benefit charge is based on amounts after line losses.”

As of November 1, 2009 the MUSH sector (Municipalities, Universities, Schools and Hospitals) and other designated institutional customers that remained as RPP customers were required to switch to non-RPP customer status as per O. Reg. 95/05 of the Ontario Energy Board Act, 1998. In response to Board staff interrogatories #4d, Welland indicated that the rate rider should not apply to RPP customers, and should exclude customers in the MUSH sector who had remained on RPP. Welland further noted that it “did not dispose of 1588-Global Adjustment in the 2009 Cost of Service Application. As a result, the amount in this account as of December 31, 2008 covers the variance since the inception of the Global Adjustment. During this period, the MUSH sector was billed as RPP customers. So in theory, they should not be charged a rate rider for the disposition of these amounts.”

Welland has requested that the Board review and approve the disposition of the December 31, 2008 balances of other Group 1 Deferral and Variance accounts as defined by the EDDVAR Report. The total balance of the Group 1 accounts, excluding the 1588 global adjustment sub-account is a credit of \$904,008. The 1588 global adjustment sub-account balance is a debit of \$326,955. Welland has included interest,

using the Board's prescribed interest rates, on these account balances up to April 30, 2010. Debit balances are amounts recoverable from customers.

Welland did not address any concern with respect to the impact on its cash flow were it to use the one-year default disposition period contemplated in the EDDVAR Report to clear its deferral and variance account balances. Welland has selected a 2-year disposition period in its Deferral Variance Account Workform V4.

Welland in its Manager Summary (Page 8 of Schedule 2) addressed concern with respect to the 2006 Regulatory Assets Recovery process which disposed of Welland's December 2004 deferral variance account balances combined with actual and estimated interim recoveries, actual and estimated carrying charges as well as Hydro One Low Voltage charges to April 30, 2006. Welland made note that the Board's Deferral Variance Workform "also assumes that forecast recoveries to April 30, 2006 and the associated interest contained in the 2006 EDR is also final. Any differences between forecast and actual recoveries and interest to April 30, 2006 is borne by the shareholder. As Welland Hydro has booked recoveries and interest into 1590 based on actual, this results in a difference between the amount for disposition for 1590 in the module and the balance remaining in the general ledger."

Welland included the reconciliation below and further stated that "Welland Hydro will await confirmation from the OEB before adjusting for the difference between the 1590 amount for disposition from the module and the actual amount in the general ledger."

<u>Account 1590</u>	<u>2006 EDR & 2010 IRM Deferral and Variance Module</u>	<u>Actual General Ledger</u>
Expenses/Interest to Recover	\$3,436,103	\$3,436,103
Recovery/Interest to April 30, 2006	<u>-1,756,129</u>	<u>-1,776,919</u>
Balance to Recover from May 1, 2006	\$1,679,974	\$1,659,184
Recovery from May 1, 2006	-1,690,674	-1,690,674
Interest from May 1, 2006	<u>38,837</u>	<u>37,847</u>
Balance for Disposition	<u><u>\$28,137</u></u>	<u><u>\$8,357</u></u>

In response to Board interrogatory #5c, Welland notes “as noted on Page 8 of Schedule 2 in the application, Welland Hydro has been recording recoveries at actual where they should have been based on the amounts approved by the Board in the 2006 EDR. Welland Hydro completed the 2010 Deferral & Variance module based on recoveries and interest included in the 2006 EDR up to May 1, 2006. Recoveries from May, 2006 until the rate riders were removed in 2008 were recorded as actual in the model. Welland Hydro provided an analysis of the differences between the 2010 IRM Deferral & Variance Module and the current actual general ledger on Schedule 2 Page 8 of the application. There is a small difference in the interest on the principle between the model and actual. Interest in the model is based on the principle using 2006 EDR recoveries. Actual recoveries were greater than the 2006 EDR which reduces the principle for which actual interest was calculated.”

Submission

Board staff suggests that the Board may wish to consider establishing a separate rate rider for the disposition of the global adjustment sub-account balance. The rate rider would apply prospectively to non-RPP customers, and would exclude the MUSH sector and other designated customers that were on RPP. Board staff submits that recovering the global adjustment sub-account balance solely from non-RPP customers would be more reflective of cost causality since it was that group of customers that were

undercharged by the distributor in the first place. However, the Board may wish to consider, as an alternative, to recover the allocated global adjustment sub-account balance from all customers in each class. This approach would recognize the customer migration that might occur both away from the non-RPP customer group and into the non-RPP customer group.

In addition to the decision on whether a separate rate rider should be established for the disposition of the global adjustment sub-account, the Board must decide on the time period over which the rate riders should apply. As previously noted, customer migration might occur in the low volume group. For this group of customers, there would be a benefit to dispose of the global adjustment sub-account balance over a relatively short period of time in order to reduce inter-generational inequities. Board staff submits that a disposition period no longer than one year would be appropriate. These balances have been accumulating over the last four year period and to delay immediate action is not in the customer's best interest. Board staff recognizes that some volatility in electricity bills may result. That aside, Board staff believes that a one year disposition period would be in the interest of all parties.

In order to reduce inter-generational inequities, Board staff submits that the disposition period for all Group 1 accounts should not exceed one year.

The EDDVAR Report includes filing guidelines for the disposition of deferral and variance account balances. With respect to the reliability of account balances, the EDDVAR Report at page 27 states "... The Board believes that ... additional audit certification is not necessary. The Board however will require a distributor to file a reconciliation of the regulatory trial balance that is reported to the Board as part of RRR and the audited financial statements."

Board staff notes the original balances proposed for disposition (and supported by audited financial statements) might have been adjusted to account for events

subsequent to the release of the EDDVAR Report. They include, but are not exclusive to the following:

1. The Regulatory Audit & Accounting Bulletin 200901 (“accounting bulletin”) dated October 15, 2009 and accounting frequently asked questions issued in October 2009 clarified the accounting rules for account 1588 RSVApower and global adjustment sub-account. The accounting bulletin required electricity distributors to review and correct misstatements since January 1, 2005 or since the last time Account 1588 RSVApower and global adjustment sub-account were cleared by the Board on a final basis. Due to the changes to account balances arising from the accounting bulletin Board staff asked distributors to confirm their compliance to the accounting requirements specified in the bulletin.
2. Applicants retroactively reviewing, and correcting Group 1 account balances over the January 1, 2005 to December 31, 2008 period.

Board staff notes that the final proposed balances for disposition may no longer reconcile with previously audited balances nor with Welland’s RRR filings. Board staff has reviewed the balances and notes that the changes do not result in material differences. Board staff notes that Welland stated in response to staff’s interrogatory # 5d that Welland has complied with the Board’s accounting policies and procedures. Board staff is mindful of the importance of a timely disposition of deferral and variance account balances and does not believe that the disposition should be delayed. Board staff suggests that the Board consider approving the proposed deferral and variance account balance disposition rate riders on a final basis.

On September 4, 2009 the Board issued a direction communiqué “Disposition of Residual Balance in Account 1590 for 2006 Approved Regulatory Assets”. The communiqué explained the Board’s position with respect to the differences created by distributor’s accounting transactions recorded against the deferral and variance account

post December 31, 2004 and the Board's 2006 EDR final disposition of balances. The following is excerpted from the communiqué:

"The 2006 Regulatory Assets process disposed of all balances in the regulatory asset accounts as of December 31, 2004. The 2006 Regulatory Assets process included actual and estimated amounts to April 30, 2006. The decisions for each distributor resulted in the disposition of the approved amounts by way of final rate riders and the transfer of the approved amounts to account 1590. The amounts transferred to account 1590 were disposed on a final basis and no account specific true-ups were identified as being required other than Hydro One Low Voltage ("LV") charges. Therefore, items, other than Hydro One LV charges, that relate directly to the December 31, 2004 balances such as the reconciliation of differences arising from actual versus estimated recoveries and actual versus estimated interest calculations should not be included in the workform continuity schedules.

The opening balances for all account (as of December 31, 2004) cleared in the 2006 Regulatory Assets process are deemed to be \$0 from January 1, 2005 onwards, except for account 1590. Errors, omissions and adjustments related to the 2006 Regulatory Asset process should not be included unless the distributor has received Board approval to do so.

Account 1590's opening balance is the Board approved amount as part of the 2006 Regulatory Assets process (as found on Cell C51 on sheet "2. Rate Riders Calculation" of the 2006 Regulatory Asset Recovery model) for the purpose of this workform. The only transactions that are to be shown post April 30, 2006 in account 1590 are the amounts collected from the May 1, 2006 Regulatory Assets Recovery rate rider charges and simple interest calculated on the opening monthly balances of account 1590. "

Board staff submits that the Board has clearly defined its position, being that the 2006 Regulatory Asset Recovery decision is final. Any differences between distributors recorded transactions from January 1, 2005 to April 30, 2006 with respect to disposed balances as at December 31, 2004, actual and estimated recoveries to April 30, 2006, actual and estimated interest to April 30, 2006 and the Hydro One Low Voltage charges including related interest are not to be included for further disposition in Account 1590. Board staff suggests that the Board may wish to direct Welland not to include the differences noted above in the final balance of Account 1590 for disposition in this proceeding.

TREATMENT OF SMART METER FUNDING ADDER

Background

Welland has a current Board-approved smart meter funding adder of \$0.27 per month per metered customer. In its application, Welland is requesting an increase in its rate adder to \$1.81 per month per metered customer. Welland filed evidence in accordance with section 1.4 of the Guideline G-2008-0002: Smart Meter Funding and Cost Recovery (the "Smart Meter Guideline"), issued October 22, 2008. Welland is authorized for smart meter deployment under the amended Regulation pursuant to and in compliance with the London Hydro RFP process.

Welland is not seeking approval for capital and operating costs incurred to date or in 2010 in this application, but will track actual costs, and revenues received from the funding adder, in the established deferral accounts for review and disposition in a subsequent application.

Submission

Board staff submits that Welland has complied with the policies and filing requirements of the Smart Meter Guideline. Actual smart meter expenditures will be subject to review

when Welland makes application for disposition of the account balances in a subsequent proceeding. Hence, Board staff takes no issue with Welland's proposal to increase its smart meter funding adder to \$1.81 per month per metered customer.

ADJUSTMENTS TO THE REVENUE TO COST RATIOS

Background

The Board's Decision (EB-2008-0247) for Welland's 2009 cost of service rate application prescribed a phase-in period to adjust revenue to cost ratios. The 2010 Supplemental Filing Module included schedules for Welland to complete to address this matter. The process adjusts base distribution rates before the application of the price cap adjustment.

Submission

Board staff submits that Welland has complied with the filing requirements of the 2010 Supplemental Filing Module. Board staff takes no issue with Welland's revenue to cost ratio adjustments.

ADJUSTMENTS TO THE RETAIL TRANSMISSION SERVICE RATES (RTSR)

General Background

Electricity transmitters in Ontario charge Uniform Transmission Rates (UTR) to their transmission connected customers. These UTRs are charged for network, line connection and transformation connection services. Based on the Decision and Rate Order of the Board in the EB-2008-0272 proceeding, the new UTRs effective July 1, 2009 were as follows:

- Network Service Rate was increased from \$2.57 to \$2.66 per kW per month, a 3.5% increase;

- Line Connection Service Rate remained unchanged at \$0.70 per kW per month; and
- Transformation Connection Service Rate was decreased from \$1.62 to \$1.57 per kW per month, for a combined Line and Transformation Connection Service Rates reduction of 2.2%.

On July 22, 2009 the Board issued an amended "Guideline for *Electricity Distribution Retail Transmission Service Rates*" ("RTSR Guideline"), which provided electricity distributors with instructions on the evidence needed, and the process to be used, to adjust Retail Transmission Service Rates ("RTSRs") to reflect the changes in the UTRs effective July 1, 2009. The Board set as a proxy at that time an increase of 3.5% for the Network Service Rate and reduction of 2.2% for the combined Line and Transformation Connection Service Rates. The Board also noted that there would be further changes to the UTRs in January 2010.

Based on the Decision and Rate Order of the Board in the EB-2008-0272 proceeding, a Rate Order issued January 21, 2010 revised the UTRs effective January 1, 2010 as follows:

- Network Service Rate has increased from \$2.66 to \$2.97 per kW per month, an 11.7% increase over the July 1, 2009 level or 15.6% over the rate in effect prior to July 1, 2009;
- Line Connection Service Rate has increased from \$0.70 to \$0.73 per kW per month; and
- Transformation Connection Service Rate has increased from \$1.57 to \$1.71 per kW per month, for a combined Line and Transformation Connection Service Rates increase of 7.5% over the July 1, 2009 level or 5.2% over the rate in effect prior to July 1, 2009.

Welland Specific Background

Welland has applied for an adjustment to its RTSR rates based on the July 22, 2009 RTSR Guideline proxy rate adjustments.

Submission

Board staff notes that very few distributors, including Welland, effected in their 2009 rates the July 1, 2009 level of UTRs since for most of them, distribution rates would have been implemented on May 1, 2009. Therefore, in accordance with the July 22, 2009 RTSR Guideline, Board staff submits that the revisions to the RTSRs ought to reflect the changes from the current level to the January 1, 2010 level, that is an increase of about 15.6% to the RTSR Network Service rate, and an increase of about 5.2% to the RTSR Line and Transformation Connection Service Rate.

Board staff has reviewed the evidence provided by the applicant and submits that the proposal by Welland may no longer be reasonable, based on the January 1, 2010 level of the UTRs. Board staff submits that the applicant's proposed rates be revised to reflect the January 1, 2010 values.

ACCOUNTING FOR THE IMPLEMENTATION OF THE HARMONIZED SALES TAX

General Background

The Ontario provincial sales tax ("PST") (currently at 8%) and the Federal goods and services tax ("GST") (currently at 5%) will be harmonized effective July 1, 2010, at 13%, pursuant to Ontario Bill 218 which received Royal Assent on December 15, 2009.

The PST is currently an incremental cost applied to the price of goods purchased by an electricity distributor and is included in a distributor's OM&A expenses and capital expenditures. The PST is therefore included in the distributor's revenue requirement and is recovered from ratepayers through the application of distribution rates.

When the PST and GST are harmonized, distributors will pay the HST on purchased goods and service but will now claim an input tax credit for the PST portion. The mechanics of HST as a value added tax means that the distributor will no longer incur that portion of the tax that was formerly applied as PST (i.e. the 8%) on goods purchased. However, the current rates as applied will continue to effect cost recovery as if the PST was still in place. If no action is taken, the distributor will realize a savings in the cost of goods purchased while applying rates which do not reflect those savings.

Welland Specific Background

In response to Board staff interrogatory # 8a which asked if Welland agrees that a deferral account should be established to capture the reductions in OM&A and capital expenditures, Welland stated that "Reductions in Income Taxes do form part of the IRM rate setting process. These savings are split equally between the distributor and customers. Should the Board decide to create a variance account for savings as a result of the HST the savings should be split in the same manner as Income Taxes to cover additional administrative work."

Submission

Board staff notes that many distributors' comments on the administrative burden and costs of sales tax harmonization are at odds with the provincial and Federal governments' pronouncements regarding the stimulative and competitive results of harmonization. Because the costs and savings are not clear at this point, Board staff submits that tracking of these is warranted at this point to quantify, per government pronouncements, that the potential savings for corporations like Welland could be significant. Accordingly, Board staff submits that the Board may wish to consider establishing a deferral account to record the amounts, after July 1, 2010 and until Welland's next cost-of-service rebasing application, that were formerly incorporated as the 8% PST on capital expenditures and expenses incurred, but which will now be eligible for an HST Input Tax Credit ("ITC"). The intention of this account would be to

track the incremental change due to the introduction of the HST that incorporates an ITC from the 5% to the 13% level. To qualify for this treatment, the cost of the subject items must be in the category of distribution revenue requirement. Tracking of these amounts would continue in the deferral account until Welland's next cost of service application is determined by the Board or until the Board provides guidance on this matter, whichever occurs first.

Welland would apply to clear the balance in the account as a credit to customers at the next opportunity for a rate change after the account balance information becomes available and is supported by audited financial statements.

All of which is respectfully submitted