The Voice Of Ontario's Electricity Distributors

August 14, 2006

Board Secretary
Ontario Energy Board
2300 Yonge Street
Suite 2700
Toronto, ON   M4P 1E4

Via email to BoardSec@oeb.gov.on.ca and by courier

Dear Board Secretary:

Re: Expert Report and comments on the OEB Staff Discussion Paper: Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors: file numbers EB-2006-0088 (Cost of Capital) and EB-2006-0089 (2nd Generation IRM)

The Electricity Distributors Association ("EDA") is the voice of Ontario's electricity distributors. Enclosed is an expert report, inclusive of the EDA's comments on the OEB Staff Discussion Paper, prepared for the EDA by Christensen Associates Energy Consulting in response to the Board's invitation to interested parties to make their submissions on the determination of Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors.

Please direct any questions or comments to Guru Kalyanraman at 905.265.5334 or at gkalyanraman@eda-on.ca.

Yours truly,

C.C. (Charlie) Macaluso
President and Chief Executive Officer

Encl.

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Additional EDA Comments on OEB Staff Discussion Paper

Smart Meter Funding

In the Staff Discussion Paper that was released July 25, 2006, OEB staff is proposing an increase in 2007 of $1 to the fixed distribution rate of distributors currently working to achieve the government's target of smart meter installations (800,000) for the end of 2007 (i.e., Toronto Hydro-Electric System Limited, PowerStream Inc., Enersource Hydro Mississauga Inc., Veridian Connections Inc., Hydro Ottawa Limited, Horizon Utilities Corporation, Newmarket Hydro Ltd., Milton Hydro Distribution Inc., and Chatham-Kent Hydro Inc). Similarly, OEB staff is also proposing an increase in 2007 of 30 cents to the fixed distribution rate of the remaining distributors that will have obligations to meet the government's 2010 target for smart meter installations.

The six large distributors are currently working in an RFPQ process. The Ministry of Energy has expressly provided that all other LDCs be given the option of 'piggyback' with the large utilities or Hydro One in order to procure meters. It is anticipated that a number of LDCs may choose to piggyback with these large distributors or Hydro One in the ongoing procurement process for smart meters. The initial procurement of smart meters would take place in Fall of this year. LDCs that choose to piggyback with these large distributors in procuring smart meters will not have adequate funding through their OEB allowed revenue requirement to fund procurement, as they have been provided with only a $ 0.30 funding per smart meter per month for their smart meters. In order to ensue that the 'piggybacking' option intended to be given to all LDCs is a <u>real</u> option available to utilities, fulsome funding must be made available. The OEB Staff proposal to provide only an additional $ 0.30 for the remaining distributors in 2007 could thus continue to be a barrier to the smart meter installation for many LDCs who would like to piggyback with the larger LDCs or Hydro One. The insufficiency of funding could force LDCs not to move forward on the procurement of meters at this time.

Determination of Working Capital Allowance

The 2006 EDR Handbook provides for a maximum of 15% of cost of power plus controllable expenses as working capital allowance. In the 2006 EDR the working capital allowance was included in the calculation of the LDC's rate base and thus allowed a rate of return. In the Draft Staff Report, released by the OEB in June 2006, OEB staff proposed that the working capital should be allowed a short term debt rate consistent with the allowed rates for variance and deferral accounts of one year. Later, in the Staff Discussion Paper, released in July 2006, OEB staff proposed as an option that short-term debt, needed to finance working capital, be deemed to be 8% of rate base.

Should the working capital allowance of LDCs be limited only to 8% of rate base, as opposed to the current practice of including a maximum of 15% of cost of power plus controllable expenses as working capital allowance, it would result in a reduction in the revenue requirements for LDCs and have an impact on the cash flow stability, as LDCs use their working capital to 'bridge finance' the period between their payments to the IESO and the point at which they are fully reimbursed by end-users through the billing process.