July 19, 2007

Ms. Kristen Walli
Board Secretary
Ontario Energy Board
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Subject: Board Staff Discussion Paper On the implications arising from a review of the electricity distributors' cost allocation filings. (the "Staff Discussion Paper") EB-2007-0667

These comments are provided on behalf of Enersource Hydro Mississauga Inc., Horizon Utilities Corporation, Hydro Ottawa Limited, PowerStream Inc., Toronto Hydro-Electric System Limited and Veridian Connections Inc., collectively referred to herein as the Coalition of Large Distributors ("CLD").

Local Distribution Companies (LDCs) were required to file cost allocation studies based on the Ontario Energy Board's (the "Board's") "*Cost Allocation Review: Board Directions on Cost Allocation Methodology for Electricity Distributors. EB-2006-0317, September 29, 2006*" (the "Policy") and the Cost Allocation Model (the "Model").

In their paper, Board staff describe using a statistical approach (frequency ranges) and sensitivity analyses (varying the customer related costs) to establish a suggested range of acceptable revenue to cost ratios. Staff's statistical analysis was used primarily for the Residential and GS < 50 kW classes where the ranges of revenue to cost ratios for those utilities which filed were tightest and most uniform. For the other classes, Board Staff relied on sensitivity analysis for ten medium customer-density utilities. In the CLD's view it is not a "given" that the conclusions reached by Board Staff for this group would also be applicable to low density and high density utilities.

The results of the sensitivity analysis, Table 1 on page 13, highlight that there are issues with the use of the minimum system, especially for the classes with larger customers. (See further comments on this topic below).

Transformer Ownership Credits

The CLD has serious concerns about how the current Cost Allocation Model handles the Transformer Ownership credits. Several members of the CLD highlighted this concern in their filings and provided information on the extent to which the revenue to cost ratios were affected.

For instance Toronto Hydro stated at page 5 of 8 of their EB-2006-0247 filing that:

> "In working with the model and reviewing the model results, Toronto Hydro believes that there are fundamental flaws in the way that transformation costs

and the transformer allowance are applied. These flaws result in distortions of the revenue to cost ratios, first of all because allocated costs are compared to gross revenues by class, unadjusted for the transformer allowance.

Secondly, in the current version of the model, there can be a mis-match between the transformer allowance costs allocated to a given class and the transformer allowance actually paid to that class."

The Cost Allocation Model allocates the Transformer Ownership Credits as costs to Transformer O&M USoA accounts, which are spread across all customer classes that require LDC transformation. The resulting impact is that customer classes are allocated very significant costs incorrectly and inappropriately. The problem is often exacerbated for the Large User Class in which most, if not all, customers own their own transformers and therefore currently receive a transformer ownership credit.

The model should be adjusted so that the transformer ownership credits are not added back to Transformer O&M costs. In addition the class revenue reported in the Customer data should be adjusted so that it is net of the transformer ownership credit. These changes would have a significant impact in the revenue to cost ratios. For instance, Horizon made these adjustments to their cost allocation model and the revenue to cost ratio for the Large User Customer Class dropped from 98% to 50% and increased from 118% to 124% for the Residential Customer Class, these adjustments were not however, filed with the Board but commented on in the Manager's Summary. This issue must be addressed.

What is the appropriate range for the revenue to cost ratio for customer classes?

Board staff is recommending that the following class specific revenue to cost ratio ranges be considered acceptable for the short term. This is compared with the ranges experienced by the CLD in the following table:

Class	Proposed Acceptable Range	CLD Range Run 1	CLD Range Run 2
Residential	80% to 120%	83% to 118%	83% to 118%
GS < 50 kW	80% to 120%	86% to 139%	86% to 115%
GS > 50 kW	80% to 180%	76% to 185%	76% to 142%
Large User	80% to 180%	76% to 138%	82% to 137%
USL	80% to 120%	35% to 150%	35% to 150%
Sentinel Lights	70% to 120%	14% to 39%	29% to 39%
Street Lighting	70% to 120%	10% to 81%	10% to 68%
GS TOU[1]	80% to 180%	57% to 173%	68% to 175%

[1] This class is called GS TOU for ease of comparison. In all cases it includes a class between 50 kW and 5000kW but the size is not always consistent amongst the CLD.

If these ranges are accepted by the Board, there are different implications to the CLD. All members would require an increase to the revenue from the Street light and Sentinel light (where applicable) classes. Following is the range of distribution rate increases that would be required for the Street light and Sentinel light classes.

Class	CLD Range of Increase to Distribution Rates
Sentinel Lights	13% to 450%
Street Lighting	8% to 572%

The CLD is concerned that the increase to Street Lighting distribution rates would be a significant impact on municipalities. It would appear from Figure 8 on page 21 that there would be other municipalities negatively affected as well. A number of CLD members indicated in their Cost Allocation filings their concerns that the streetlighting class was assigned service and customer related costs which likely over-represent costs associated with this class.

One method of possibly reducing any large impact on the Street Lighting class for some municipalities would be to address the cost of power issue for street lighting at the same time. Many municipalities are concerned that they are being charged for the commodity on the Regulated Price Plan, which is higher than if they were being charged based on the spot market. This is because street lights use most of their power during off peak periods when the price is lower. Street lights have not generally been eligible for the spot market price because they do not have an interval meter as required by O. Reg. 95/05 of the *Ontario Energy Board Act*. If the Board could streamline the process for municipalities to obtain approval to be billed on the spot market price, this could more than offset the potential distribution rate increase.

The CLD is also concerned about the impact on Sentinel Light customers and would suggest that this is one case where there is sufficient justification to allow the revenue to cost ratio to remain as is. Sentinel light programs are typically small and are often offered on a “grandfathered” basis. Some LDCs, such as Hydro Ottawa and Veridian Connections, no longer allow new Sentinel lights to be installed. Although the revenue adjustment required to bring the Sentinel lights’ revenue to cost ratio into the acceptable range is small in terms of the other classes’ total distribution revenue, it is large in relation to the total distribution revenue currently received from the Sentinel light class.

The implications of the Board staff proposal for ranges of acceptable revenue to cost ratios are different for each member of the CLD. As discussed previously, all members of the CLD have Street Light revenue to cost ratios outside of the suggested ranges. For those members that have Sentinel Light classes, these classes are also all outside of the suggested ranges.

- For Hydro Ottawa no other customer classes are outside of the ranges proposed by Board staff.

- For Veridian, both the General Service < 50 kW and General Service > 50 kW classes in the Gravenhurst service territory would require adjustment to conform to the proposed ranges.
- For PowerStream the GS TOU class would have to be adjusted significantly to fall with the proposed range.
- For Horizon both the Large User and GS > 50 kW classes are outside of the Board staff suggested ranges.
- For Enersource the Large Use and, potentially the USL classes are outside of the Board staff suggested ranges.
- For Toronto Hydro the USL class would see significant increases in rates if required to conform to the suggested minimum.

Implementing any of these adjustments while maintaining overall revenue neutrality would, of course, have impacts on rates for the remaining customer classes.

Board Staff's discussion paper, in providing a high level analysis of the filing results, is a good beginning in the process of developing cost based rates. The CLD believes that the results are valuable in informing LDC's on cost allocation and rate design in their rebasing exercises over the next three years. Clearly however, the results themselves show significant differences amongst LDC's without any analysis as to why the results are what they are. Board Staff indicated in the paper that the variations might be the results of "non-consistent understanding of the fundamentals associated with the methodology and the Model, or errors in the data from individual distributors". If the suggested ranges are adopted, the impacts on at least some rate classes in all jurisdictions are significant. The CLD suggests the Board should move cautiously in its implementation of any conclusions.

Furthermore, Staff's paper suggests that the ranges be applied for the short-term. It is not clear what the time frame of "short-term" is, either for implementation or continued existence of the ranges.

What is the appropriate cost range to test the fixed monthly customer charge?

Board staff is recommending that the floor for the monthly fixed charge be determined using the avoided costs. Board staff is also recommending that the ceiling for the monthly fixed charge be determined using 20% above the ceiling determined by the direct costs plus the customer related portion of the revenue requirement of poles, lines and transformers, which is determined using the minimum system method.

The minimum system is a concept that assumes that a minimum-size distribution system can be built to serve the minimum load requirement of the customer (e.g. 100 Watt lightbulb). This has been a long-standing methodology for cost allocation studies. However, Board staff is now proposing that this methodology also be used for what is essentially a rate-design issue;

determining the floor and ceiling for fixed charges. Cost allocation studies are for the purpose of allocating costs to customer classes and thereby determining the percentage of the total distribution revenue that should be realized from each specific class. These studies should not be used in isolation of other factors to make determinations on rate design. Therefore, the CLD strongly recommends that the Board staff proposal not be adopted. Instead, the issue of the appropriate split between fixed and variable distribution charges should be moved to the Board's proceeding EB-2007-0031 Rate Design for Electricity Distributors in which the Board is considering rate design issues. As a rate design issue, the CLD has many further comments to provide on the appropriate mix of fixed and variable rates, but that would appear out of scope of a review of cost allocation filings.

Should the establishment of a USL metering credit be based on an individual utility's costs?

Board staff is proposing that the establishment of metering costs for Unmetered Scattered Load ("USL") be assessed on each distributor's application and not per a provincial average. This will ensure that any cost differences between LDCs are appropriately reflected. However, this is only applicable to LDCs that do not have a specific USL rate. Those that have a specific USL rate did not include meter costs in the cost allocation to this class.

Should the establishment of a transformer credit be based on an individual utility's costs?

Board staff is proposing that the transformer credit be set for each distributor based on their costs. The CLD agrees with this proposal because this consistent with the principle of cost based rates.

Should the determination of appropriate Stand-by rates for customers with load displacement generation be based on an individual utility's costs?

Board staff is proposing that the determination of a stand-by rate for customers with load displacement generation be set on each distributor's application. The CLD agrees with this proposal because it will align rates with the LDC's costs.

The Policy outlined that a standard methodology across all utilities would be desirable to deal with customers with load displacement, and this is still a desirable goal. In addition, the issues of rates for distributed generation and standby rates for reserved system capacity for load customers still need to be addressed. The CLD notes that a Staff Discussion paper was issued by the Board on July 13, 2007 seeking comments on standby rates for load displacement generation as part of proceeding EB-2007-0630. This would appear to be the appropriate forum for addressing this matter.

Sufficiency of input data

The CLD agrees that going forward it would be desirable to establish sub-account structures that align with the requirements of the cost allocation model as well as other Board-required reporting. It should be recognized however that it would take time, effort and cost for LDCs to incorporate the required sub-accounts into their financial systems and it is crucial that definitive definitions be agreed upon by participants (e.g. subtransmission). The CLD believes that the Board should play a key role (in consultation with LDC's) in developing, clearly defining, and communicating appropriate regulatory accounting structures.

Timing

As outlined in the *Filing Requirements for Transmission and Distribution Applications, (EB-2006-0170) November 14, 2006* an applicant is required to file historical and test year revenue to cost ratios. For 2008 Distribution Rates 1st tranche filers, due on August 15, 2007, the Staff Discussion Paper provides some guidance on changes that may be required for the filing. However, given the timing of Staff's discussion paper and the fact that any final directions from the Board are yet to be issued, it is unlikely that there is sufficient time to incorporate any changes in time for initial filings. Furthermore, guidance should not change in the future for 2009 and 2010 distribution rate application filers.

Thank you for this opportunity to provide input. We would be happy to provide further clarification of these issues.

Yours truly,

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On behalf of the CLD.