London Hydro

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ONTARIO ENERGY BOARD

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Re: EB-2007-0667 – Staff Discussion Paper on the Implications Arising from a Review of the Electricity Distributors' Cost Allocation Filings

In accordance with the Board's instructions of June 28, 2007 we are providing our written comments on the Board staff's discussion paper on the Implications Arising from a Review of the Electricity Distributors' Cost Allocation Filings.

Specific Questions Asked by Board Staff in their paper:

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

Comments

Based upon the data presented in the staff discussion paper, the revenue to cost ranges might appear to be reasonable for short term usage but we would suggest that single revenue to cost ratio range of 80% to 120% should be applied to all classes.

The use of different ranges for specific customer classes implies a level of accommodation or potential cross subsidization that should not be applied in any future rate setting process.

The range of output and results from the cost allocation model are due to the many assumptions, estimates and application of certain methodologies but all customer classes are affected by these uncertainties. It is difficult if not impossible to substantiate how these factors might affect one class more than another and as a result provide the reasoning to apply different revenue to cost ratios for certain customer classes.

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

Comments

Board staffs discussion of and proposals for fixed monthly charge values should not be a component of this discussion paper. These discussions and proposals must be combined with the current initiative underway by the Board with respect to EB-2007-0031 Staff Discussion Paper on Rate Design for Electricity Distributors.

As outlined in the EB-2007-0031 discussion paper, there are certain regulatory principles that must be achieved when establishing rate structures. The rate structures must be, Practical, Clear, Effective, Stable for the utility, Stable for the customers, Fair, Promote efficient use of resources, and Avoid undue discrimination.

In this discussion paper EB-2007-0667, staff has not provided any indications as to how their proposals on fixed monthly charge values will impact the Boards stated regulatory rate setting principles, in particular the following principles:

- Effective – rates should recover the revenue requirement
- Stable for the utility – the utility should be able to recover its revenue each year without excessive profits or losses
- Stable for the customers – rates should be predictable enough for customers to make investment decisions

The minimum fixed charge values proposed by Board staff, referred to as "avoided costs" may have certain theoretical application and support, but from a practical use perspective in the function of rate design and revenue recovery their usage is not practical.

The avoided costs are defined as those costs that would be "avoided if the customer had simply never become a customer in the first place". These costs are defined as only meter related costs and billing and collection costs. This definition has certain practical usages within the cost allocation model for the purpose of assigning system infrastructure costs to customer classes, but if is to be used as a determinant in the calculation of a monthly fixed charge for revenue recovery purposes, it clearly results in virtually all of the distributors total revenue requirement being recovered through a variable rate component.

The maximum fixed charge recommended by Board staff is essentially the "minimum system cost" plus 20%. From the distributor's perspective, the investment required to design and build a minimum system is not the theoretical values derived in the cost allocation model for the purpose of determining customer class revenue requirements.

The actual minimum system is that which will provide sufficient capacity to meet the average actual demands by customer class. These actual demands are several multiples of the values used for minimum system determination, and as such the maximum monthly fixed charges proposed by staff are inadequate in terms of providing a fixed revenue recovery component that would recover the cost of the distributor's actual minimum system.

Board staff's proposals for fixed monthly charges will result in some substantial adjustments to fixed charges for certain customer classes, and while the class revenues may remain constant, there is potential for significant individual customer bill impacts within those customer classes.

In addition to individual customer bill impacts, adjustments to the fixed monthly charges will for some distributors increase the risk of revenue recovery by increasing the variable revenue components.

In the case of London Hydro, we have estimated that the ceilings for fixed monthly charges proposed by Board staff would reduce the current fixed revenue component from 49% to 34% of total revenue, thus exposing 66% of the utilities revenues to the influences of economy, weather and energy conservation.

Before proposing any adjustments to the fixed and variable rate components, Board staff should undertake a more detailed review of the impacts of such changes on individual customer bills and on the distributor's total fixed and variable revenues. Additionally, this review should analyze the existing revenues by customer class on a fixed and variable percentage basis, and the impacts of such proposals on these fixed and variable splits by customer class.

The establishment of fixed and variable rates should be more closely aligned with the actual fixed and variable cost structures of distributors versus staff's proposal to adopt fixed monthly charges that reflect the theoretical costs of a minimum system design. The purpose of the minimum system methodology was to allocate distribution system costs to customer classes to determine revenue requirements by class, not to develop a fixed monthly rate based on a non existent theoretical system.

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

Comments

For most distributors, the distribution revenues derived from USL represent a relatively minor portion (less than 1%) of their overall revenue requirement, and we believe that given a choice, distributors would prefer to have a generic metering credit value that could be applied for rate setting purposes.

To avoid the unproductive assignment of distributor resources to the development and filing of evidence to support specific metering credits for USL, we would recommend the