



EB-2007- 0794

IN THE MATTER OF the *Ontario Energy Board Act*,
1998, S.O. 1998, c.15 (Schedule B);

AND IN THE MATTER OF an application by North
Bay Hydro for an order or orders approving or fixing
just and reasonable distribution rates and other
charges, to be effective May 1, 2008.

BEFORE: Paul Vlahos
Presiding Member

Paul Sommerville
Member

DECISION

Introduction

North Bay Hydro (“North Bay”) is a licensed distributor of electricity providing service to consumers within its licensed service area. North Bay filed an application with the Ontario Energy Board (the “Board”) on November 2, 2007 for an order or orders approving or fixing just and reasonable rates for the distribution of electricity and other charges, to be effective May 1, 2008.

North Bay is one of over 80 electricity distributors in Ontario that are regulated by the Board. In 2006, the Board announced the establishment of a multi-year electricity distribution rate-setting plan for the years 2007-2010. As part of the plan, North Bay is one of the electricity distributors to have its rates adjusted for 2008 on the basis of the 2nd Generation Incentive Rate Mechanism (“IRM”) process.

To streamline the process for the approval of distribution rates and charges for distributors, the Board issued its *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors* (the "Report") on December 20, 2006. Among other things, the Report contained the relevant guidelines for 2008 rate adjustments (the "Guidelines") for distributors applying for rate adjustments pursuant to the IRM process.

Notice of North Bay's rate application was given through newspaper publication in North Bay's service area advising of the availability of the rate application and advising how interested parties may intervene in the proceeding or comment on the application. The School Energy Coalition ("SEC") applied and was granted intervenor status in this proceeding. SEC did not submit written interrogatories or submissions on the application. The Board proceeded by way of written hearing. Board staff actively participated in the proceeding.

While the Board has considered the entire record in this rate application, it has made reference only to such evidence as is necessary to provide context to its findings.

Price Cap Index Adjustment

North Bay's rate application was filed on the basis of the Guidelines. In fixing new rates and charges for North Bay, the Board has applied the policies described in the Report.

As outlined in the Report, distribution rates under the 2nd Generation IRM are to be adjusted by a price escalator less a productivity factor (X-factor) of 1.0%. Based on the final 2007 data published by Statistics Canada, the Board has established the price escalator to be 2.1%. The resulting price cap index adjustment is therefore 1.1%. The rate model was adjusted to reflect the newly calculated price cap adjustment. This price cap index adjustment applies to distribution rates (fixed and variable charges) uniformly across all customer classes. An adjustment for the transition to a common deemed capital structure of 60% debt and 40% equity was also effected. In addition, a change in the federal income tax rate effective January 1, 2008 was also incorporated into the rate model and reflected in distribution rates.

The Board also considered the reduction in Ontario capital tax and the increase in capital cost allowance (CCA) applicable to certain buildings and computers acquired

after March 2007. The Board has decided that adjustments related to these items are not required, either because the changes are not of general application, or because they do not appear to be material.

The price cap index adjustment does not apply to the following components of the rates:

- the specific service charges;
- the smart meter rate adder (an amount in the fixed components of the rates associated with smart meter cost recovery); and
- any continuing rate riders.

Accordingly, the Board is providing North Bay with a rate model (spreadsheet) that reflects the price cap adjustments described above. North Bay is required to review the rate model (spreadsheet) and to confirm its completeness and accuracy with the Board at the time it files its Draft Rate Order. North Bay shall file with the Board a Draft Rate Order attaching the proposed Tariff of Rates and Charges which will reflect the Board's price cap adjustments as verified by North Bay and any other Board findings contained in this decision that would impact 2008 rates. North Bay shall also provide the rate model (spreadsheet) that underpins the Tariff of Rates and Charges. Any changes to the Board's rate model (spreadsheet) shall be clearly identified and explained.

Rate Riders

When the Board approved new rates for distributors for 2006, it also approved the recovery of regulatory asset balances on a final basis. The Board approved rate riders to facilitate the recovery of the approved balances over the two remaining years of the four-year recovery period mandated by the Minister of Energy (i.e. May 1, 2004 to April 30, 2008). The rate rider(s) associated with the recovery of regulatory assets will cease on May 1, 2008 and shall be removed from the Tariff of Rates and Charges, unless a previous Board decision authorized the continuation of such riders beyond April 30, 2008. No such authorization has been previously provided by the Board for North Bay. The final balance in account 1590 cannot be confirmed until after the current recovery period has expired, i.e. after April 30, 2008. Once the residual balance in deferral account 1590 is finalized, the residual balance will be disposed in a future proceeding.

Smart Meter Rate Adder

North Bay requested the continuation of the smart meter rate adder previously approved by the Board in order to provide funding for possible future implementation of smart meter costs and to minimize future rate impacts. The Board-approved rate adder for North Bay of \$0.26 per month per metered customer shall continue. North Bay's variance accounts for smart meter program implementation costs, previously authorized by the Board, shall also be continued.

Z-factor Request

North Bay's application includes a request for Z factor recovery for costs relating to a severe storm which occurred on July 17, 2006. The storm interrupted service to approximately 95% of North Bay's customers. Restoration of service took several days and required North Bay to enlist the assistance of neighbouring utilities and private contractors.

In its application North Bay requested recovery in the amount of \$470,047 in the form of a rate rider adjustment of \$0.65 per month per customer over a 24 month period and deferral of these expenses to account 1572, Extraordinary Event Costs.

In response to Board staff submissions North Bay revised its total claim to \$461,119. to reflect removal of overhead for incremental engineering costs and forgoing carrying charges on the second year of its proposed 24 month recovery period. In that way, North Bay's interest recovery would be limited in time to a period over which interest would have been recovered had North Bay made its Z factor adjustment request in conjunction with its 2007 IRM application.

In considering North Bay's request for Z factor recovery the Board considered the Report which makes provisions for Z factors and outlines the guidelines for distributors applying for this type of adjustment. In the Report, the Board limits Z factors to changes in tax rules and to natural disasters. The Board recognizes extraordinary events outside the control of management but limits the reliance on Z factors to these well-defined and well-justified cases only.

The Report also provides guidance with respect to when claims for Z factors should be made. More specifically, the Report provides that in support of a proposed rate

adjustment related to Z factor amounts, a distributor must indicate the amounts booked to these accounts in the previous year and provide evidence that these amounts satisfy the criteria of causation, materiality and prudence.¹ The Board notes that the Report contemplates that a Z factor claimed for damage in 2006 should be claimed in 2007. Recognizing that storm damage can occur at any time the Report also stipulates that the Board may review and adjust Z factor amounts at any time during the term of the incentive regulation plan in order to allow the Board the flexibility to address extraordinary events in a timely manner.

In response to Board staff's interrogatories, North Bay explained that it did not seek recovery of storm costs incurred in 2006 as part of its 2007 IRM application, because North Bay only "became aware" that this was an option that could be exercised with the advent of the combined proceeding on storm damage cost claims. (EB-2007-0514, EB-2007-0595, EB-2007-0571, EB-2007-0551). This hearing, which was preceded by specific Notice to affected ratepayers, and publication on the Board's website, was held at the Board's offices on June 1, 2007.

In that case, Canadian Niagara Power Inc. – Fort Erie, Canadian Niagara Power Inc. – Port Colborne, Peterborough Distribution Inc., and Lakeland Power Distribution Ltd. requested recovery of costs associated with separate incidents of extraordinary storm damage incurred in 2006. These claims were made through the Z factor recovery mechanism outlined in the Report. By Decision with Reasons dated July 31, 2007 the Board authorized each of the distribution company applicants to establish a rate rider to recover the costs associated with their respective storm incidents in 2006.

In defence of its lateness in advancing its claim in this case North Bay also submitted that, even if it were aware of its option to make application to the Board, it would have been difficult for it to have prepared its Z factor claim in time for inclusion in its 2007 IRM claim in any event because it had attempted to secure disaster relief funding through the municipality by applying for a disaster area designation under the Ontario Disaster Relief Assistance Program. In December 2006 North Bay was advised that the Government had rejected its claim for financial assistance.

The Board does not accept North Bay's reasons for not making its request earlier. It does not provide justification for the deviation from the requirement that Z factor requests are to be made in a timely manner.

¹ Appendix C to the Board Report

However, despite the above, the Board also recognizes that the language used in the Report is less clear than it could have been with respect to when the Board can review and adjust amounts claimed under Z factor treatment. More specifically, the Report provides that:

“The Board may review and adjust the amounts claimed under Z factor treatment at any time during the term of the incentive regulation plan. This will allow the Board and any affected distributor the flexibility to address extraordinary events in a timely manner.”²

A utility may take the position that in light of the above, a utility is allowed to bring a Z factor claim at any time during the term of the incentive regulation plan. This is not the view taken by the Board. When the above is read in conjunction with the requirement that distributors must indicate the amounts booked to Z factor accounts in the previous year in support of a rate adjustment, the Board is of the view that the Report contemplates a Z factor to be claimed at the first available opportunity by the utility. One of the important principles guiding all of the Board’s work in ratemaking concerns the timeliness of rate proposals. Ratepayers are entitled to have rates set reflecting costs incurred within the period proximate to the rate period to avoid or mitigate inter-generational inequities.

Given the lack of clarity and lack of explicit guidance on the timing of making Z factor claims, rather than denying North Bay’s request in the very specific circumstances of this case, the Board is prepared to accede to North Bay’s request for Z factor recovery, and the Board so finds. On a going forward basis, utilities are expected to make any request for Z factor recovery in a timely manner which, in the Board’s view means, at the first available rate adjustment opportunity.

The Board accepts the allocation of the approved storm costs of \$461,119 based on the number of customers (using North Bay 2006 EDR customer count), and its recovery through a rate rider over a two-year period. The Board directs North Bay to recalculate the rate rider accordingly, and to include the rate rider in its rate model (spreadsheet) to be filed with the Board.

The Board notes that the claim included capital costs of \$41,898 related to distribution transformers. The Board allows the recovery of the total cost as operating expenses.

² Section 3.5 of the Board Report.

Therefore, North Bay should not capitalize any of the approved costs for rate base purposes, nor should any approved costs be treated as distribution expenses for the purpose of determining a future revenue requirement.

Retail Transmission Service Rates

On October 17, 2007, the Board issued its EB-2007-0759 Rate Order setting new Uniform Transmission Rates for Ontario transmitters, effective November 1, 2007. The Board approved a decrease of 18% to the wholesale transmission network rate, a decrease of 28% to the wholesale transmission line connection rate, and an increase of 7% to the wholesale transformation connection rate. The combined change in the wholesale transmission line connection and transformation connection rates is reduction to the connection rate of 5%.

On October 29, 2007, the Board issued a letter to all electricity distributors directing them to propose an adjustment to their retail transmission service (RTS) rates to reflect the new Uniform Transmission Rates for Ontario transmitters effective November 1, 2007. The objective of resetting the rates was to minimize the prospective balance in variance accounts 1584 and 1586 and also to mitigate intergenerational inequities.

North Bay did not file a proposal to adjust its RTS rates and indicated that it will undertake to file a separate application in this regard. Given the magnitude of the changes in wholesale transmission rates, the Board directs North Bay to reduce its RTS – Network Service Rates by 18% and its RTS – Line and Transformation connection Service Rates by 5%. North Bay is required to include these changes in its rate model (spreadsheet) to be filed with the Board.

Implementation

North Bay's new distribution rates are effective May 1, 2008. The Board directs that:

1. North Bay shall file with the Board, and shall also provide SEC a copy of, a Draft Rate Order attaching the proposed Tariff of Rates and Charges and the supporting rate model (spreadsheet) within seven (7) days of the date of this Decision. The proposed Tariff of Rates and Charges shall be filed in a Word format. The adjusted rate model shall be filed in an Excel format.

2. SEC shall file any comments on the Draft Rate Order with the Board and forward to North Bay within fourteen (14) days of the date of this Decision.
3. North Bay shall file with the Board and forward to SEC responses to any comments and revisions to the Draft Rate Order within seventeen (17) days of the date of this Decision.

DATED at Toronto, March 19, 2008.

Original signed by

Paul Vlahos
Presiding Member

Original signed by

Paul Sommerville
Member