**Ontario Energy Board**

**Commission de l'Énergie de l'Ontario**

Ontario

**EB-2008-0236**

**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 Midland Power Utility Corporation for an order approving or fixing just and reasonable rates and other charges for the distribution of electricity to be effective May 1, 2009.

**BEFORE:** **Cynthia Chaplin**
Presiding Member

**Paul Sommerville**
Member

**DECISION AND ORDER**

May 12, 2009

**BACKGROUND**

Midland Power Utility Corporation ("Midland") filed an application with the Ontario Energy Board on August 15, 2008, under section 78 of the *Ontario Energy Board Act, 1998*, seeking approval for changes to the rates that it charges for electricity distribution to be effective May 1, 2009. Midland is the licensed electricity distributor serving the Town of Midland.

Midland is one of about 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. In an effort to assist distributors in preparing their applications, the Board issued the *Filing Requirements for Transmission and Distribution Applications* on November 14, 2006. Chapter 2 of that document outlines the filing requirements for cost of service rate applications, based on a forward test year, by electricity distributors.

On January 30, 2008, as part of the plan, the Board indicated that Midland would be one of the electricity distributors to have its rates rebased for the 2009 rate year. Accordingly, Midland filed a cost of service application based on 2009 as the forward test year.

The Board assigned the application file number EB-2008-0236 and issued a Notice of Application and Hearing on September 17, 2008. The Board approved three interventions: The Association of Major Power Consumers in Ontario ("AMPCO"), School Energy Coalition ("SEC"), and Vulnerable Energy Consumers Coalition ("VECC"). Board staff also posed interrogatories and made submissions. The Board determined that this application would be conducted by way of a written hearing. The hearing closed with the filing by Midland of its reply argument on March 11, 2009.

The full record is available at the Board's offices.

In its original application, Midland requested a revenue requirement of $3,582,721 to be recovered in new rates effective May 1, 2009. The resulting requested rate increase was estimated at 8.8% over 2008 on the distribution component of the bill for a residential customer consuming 1,000 kWh per month.

In its final submission, Midland agreed with a number of adjustments to its application and revised its revenue requirement to $3,392,787.

The following aspects of Midland's application were accepted by all parties:

- Line Losses
- Specific Service Charges
- Retail Transmission Rates [reviewing at this time, march 31]

The Board accepts Midland's evidence on these matters and the associated rate consequences.

**THE ISSUES**

The issues listed below were raised in the submissions filed by Board staff, SEC or VECC and are addressed in the following sections of the Decision:

- Load Forecast
- Operating, Maintenance & Administrative Expenses
- Payments in Lieu of Taxes
- Rate Base and Capital Expenditures
- Smart Meters
- Cost of Capital and Capital Structure
- Cost Allocation and Rate Design
- Deferral and Variance Accounts

**LOAD FORECAST**

VECC submitted that the approach used by Midland to weather normalize historical usage and project 2008 and 2009 weather normal consumption is preferable to the methodologies used by other distributors. For the purpose of setting 2009 rates, VECC submitted that the Board should accept Midland's load and customer forecast. However, VECC claimed that there is still room for improvement and recommended that the Board direct Midland to refine its weather normalization and forecasting approach for its next rebasing application in the following ways:

- Integrate the forecasts of customer count and usage.
- Pro-rate monthly data, prior to the full availability of true monthly data based on smart metering.
- Develop a more rigorous approach for forecasting future use in the GS<50 class.

In its reply submission, Midland acknowledged that it is reasonable to expect improvements to its load forecasting methodology for the next rebasing application and indicated that it would ensure the best forecasting methodology available at that time.

**Board Findings**

The Board finds that Midland's load and customer forecast is appropriate. The Board notes that Midland has committed to ensuring it has the best available forecast methodology for its next rebasing. The Board is satisfied with this commitment and concludes that no explicit direction from the Board is required in this area.

## OPERATING, MAINTENANCE and ADMINSTRATIVE EXPENSES ("OM&A")

Table 1 below shows the five basic components of the proposed OM&A expenses for 2009 and compares them with previous years. Property and capital taxes are not included in this presentation.

**Table 1 - OM&A Expenses ($)**

| | 2006 Board Approved | 2007 Actual | 2008 Forecast | 2009 Forecast |
|---|---|---|---|---|
| **Operations** | 272,722 | 352,987 | 392,900 | 455,700 |
| **Maintenance** | 306,118 | 283,582 | 338,200 | 353,900 |
| **Billing & Collecting** | 412,100 | 451,821 | 420,400 | 435,800 |
| **Community Relations** | 15,581 | 15,073 | 5,700 | 5,600 |
| **Administrative & General** | 673,755 | 650,232 | 744,600 | 773,700 |
| **TOTAL** | **1,680,276** | **1,753,695** | **1,901,800** | **2,058,900** |

The 2009 OM&A figure reflects Midland's original proposal filed in August 2008, adjusted to remove property and capital taxes. During the course of the proceeding, Midland proposed adjustments to its original OM&A in the areas of International Financial Reporting Standards ("IFRS") and regulatory costs. Midland included a budget amount of $100,000 for the expected one-time costs of implementing IFRS. Midland proposed to amortize the amount over 4 years, so the 2009 rates would include only $25,000. No ongoing IFRS costs were included in the budget. Midland also reduced its regulatory costs to remove costs associated with an oral hearing. Midland's reply submission showed an adjusted 2009 OM&A of $2,099,350 to reflect these changes, namely an increase of $25,000 for IFRS and a total reduction of $18,750 for regulatory costs. The reduction includes the effects of both the amortization over 4 years (versus 3 years) and a decrease of $50,000 in the regulatory budget to reflect the removal of the oral component of the hearing.

The figure includes property and capital taxes of $34,200. Removing property and capital taxes yields an adjusted 2009 OM&A of $2,065,150. The increase in total OM&A expenses over the 2008 forecast is 8.6%. The increase in OM&A since the 2006 Board-approved OM&A (the last set of base rates approved by the Board) is 22.9%.

The submissions from VECC and SEC addressed OM&A increases in general, regulatory costs, inflation, and compensation costs.

While VECC noted that compensation amounts have been increasing at a rate higher than inflation, it did not take issue with the compensation component of the 2009 revenue requirement as proposed by Midland. VECC did question whether an additional manager is required for regulatory activities. VECC also argued that regulatory costs should be reduced by $25,000 because there was no oral hearing element to the application. VECC pointed out that Midland had included this amount for an oral component to the proceeding. Midland responded that its regulatory costs were in fact already reduced for the absence of an oral component to the hearing (from $175,000 to $125,000). Midland also argued that the new manager would have a variety of regulatory duties extending beyond Board related activities.

SEC took the position that the OM&A levels proposed for the 2009 Test Year were, in general, too high and that an increase of 3% for OM&A costs per customer for each of the years 2008 and 2009 would be more reasonable. SEC calculated that by doing this, the revenue requirement reduction would be about $174,400 for 2009. Midland disagreed with SEC's proposal of holding to a 3% annual increase for 2008 and 2009. Midland argued that its evidence supported the proposed increase and that its labour costs need to rise at a rate higher than 3%. Midland noted for example that its unionized labour costs will increase by 8.5% over 2008 levels. Midland also noted its need to hire an additional operations manager in 2009. Midland maintained that it requires a stable labour force, and to accomplish this, its wages must be competitive in the marketplace.

**Board Findings**

The Board notes that Midland has already reduced its regulatory costs from $175,000 to $125,000 to recognize that there was no oral component to this proceeding. The Board will make no further reduction to this amount and accepts Midland's proposal to amortize this amount over four years.

The Board currently has a process underway to consider IFRS transition and related costs. Midland has included an amount of $25,000 for a portion of its one-time expenses, but has not included any amount for ongoing expenses. The Board will accept this approach. The Board notes that Midland should continue to monitor the Board's IFRS consultation process for further developments in this area.

The Board understands SEC's concerns regarding the magnitude of OM&A increases since 2007. However, the Board finds that Midland has adequately justified its proposals and concludes that no further adjustments are warranted.

## PAYMENTS IN LIEU OF TAXES (PILs)

Board staff submitted that the appropriate regulatory income tax rate for Midland is 16.5% based on changes announced in the 2009 Federal Budget. Midland agreed.

SEC noted that the 2009 Federal Budget included changes such as additional accelerated capital cost allowance applicable to 2009 and submitted that Midland should reflect these changes in the PILs calculation. Similarly, the Government of

Ontario plans to release its 2009 budget on March 26, 2009. SEC submitted that should the budget include corporate tax reductions, Midland should include those in the final PILs calculation in the rate order. Midland responded that PILs calculations should be based on income tax rates in effect as at January 1, 2009.

**Board Findings**

The Board notes that Midland accepts that the appropriate tax rate is 16.5%.

The Board finds that the PILs allowance should be based on the most current information available. In filing its Draft Rate Order, Midland should incorporate all other known income and capital tax changes into its PILs calculations for 2009 that have arisen since the application

## RATE BASE and CAPITAL EXPENDITURES

Midland requested approval of a rate base of $12,202,110 for the 2009 Test Year. This represents an increase of 36% ($3,227,755) over 2007 actual and an increase of 45% ($3,798,482) over 2006 actual.

The following issues are addressed in this section:

- Capital Expenditures
- Working Capital Allowance

### Capital Expenditures

As noted in Table 2 below, Midland forecast capital expenditures of $2,820,000 in 2009. This is an increase of approximately 94% over 2007 actual capital expenditures and an increase of 28% over 2008 capital expenditures.

**Table 2 - Summary of Capital Expenditures 2007-2009**

| | 2007 Actual | 2008 Bridge | 2009 Test |
|---|---|---|---|
| **Capital Expenditures** | $1,451,837 | $2,209,053 | $2,820,800 |
| **% change as compared to the prior year** | | 52% | 28% |

A majority of the projects are related to replacing aging infrastructure and old vehicles or improving system reliability. One major initiative is the replacement of six substations, one per year for the years 2007 to 2010 and two in 2011. The first four substations slated for replacement are approximately 50 years old. Midland acknowledged that this plan is aggressive but considered this to be a matter impacting safety and reliability. The Fourth Street Substation upgrade at a cost of $1.2 million will be undertaken in 2009.

SEC argued that Midland had not followed the recommendations of the engineers, because the company proceeded first with the replacement of the Scott Street Substation in 2007 when the engineers identified the Fourth Street Substation as being in the worst condition. Midland replied that SEC's criticisms were unfounded. Midland pointed to the engineering consultant's letter (which accompanied the report) which specifically recommended work on the Scott Street and Brandon Street substations before the Fourth Street Substation.

Commenting on the overall capital budget, SEC noted that the 2008 forecast, excluding the substation replacement program, was $1.2 million and that the 2009 budget of $1.5 million was a 23% increase. SEC further noted that the 2009 proposed capital spending excluding the substations program was 99% higher than the comparable figure for 2007. SEC argued that the 2009 spending plan was not reasonable and submitted that the Board should approve an amount of $838,000 plus the costs related to the Fourth Street Substation for the 2009 Test Year. This would result in a total capital budget of $2,072,800 for 2009, an increase of 43% over 2007 according to SEC. SEC also did not agree with Midland's assessment that the only project that can be delayed is the SCADA project. Midland disagreed with SEC's recommendation to reduce the 2009 capital budget and submitted that the capital budget of $2,280,000 was required and should be approved.

VECC noted the significant increase in the update in 2009 capital spending for pole street rebuilds (from $406,600 to $548,600) and for vehicles (from $335,000 to $386,500).

VECC submitted that the spending on pole line rebuilds was about twelve times the $45,300 budgeted on pole projects in 2007; 2.7 times the total spending on pole line projects for 2005, 2006 and 2007 combined; and 40% higher than the projected spending on pole lines for 2010 and 2011. VECC submitted that the Board should reduce the proposed amount for these projects of $548,600 and approve the original budgeted amount of $406,600.

In Reply, Midland submitted that there was an error in its response to VECC interrogatory 21(b) with respect to grouping on pole line rebuilds. Midland indicated that it incorrectly included the Bourgeois Line Transformer Kiosk Project with the category of pole line rebuilds. If this item were excluded, the original pole line projects estimate would be reduced from $406,600 to $353,500 and the updated pole line projects estimate would be reduce from $548,600 to $405,600. Midland submitted that the increase was not 35% over the original budgeted amount as claimed by VECC, but just 15%. Midland submitted that the increased cost was warranted and requested that the Board approve the revised amount.

With respect to vehicle spending, VECC submitted that absent any credible reason for the increase in the budgeted amount, the $51,000 increase should not be allowed especially given the state of the economy. Midland responded that the bucket truck was manufactured in the United States and the increase in cost was attributed to the increase in the currency exchange rates prevailing from the time of the filing of the application to the purchase in 2009. Midland submitted that the current exchange rate had negatively impacted Midland further and it expected to pay a higher cost than the revised amount.

VECC submitted that Midland had indicated that it was “on target” to spend $2,386,653 in total capital additions for 2008[1] and yet had only spent $1,526,104 as of October 31, 2008. This implied that Midland would spend $860,549, or 36% of the total 2008 capital spending, in the final two months of the year. VECC submitted that if capital spending was even throughout the year, the projected 2008 capital spending would be $1,832,000.[2] Consequently, the 2008 capital spending should be reduced from $2,386,653 to $1,832,000 and the rate base should be adjusted accordingly.

Midland replied that VECC’s argument showed a lack of understanding about the capital scheduling process that utilities undertake during the course of a year. Midland submitted that major capital projects are designed based on when demand will accommodate the disruption and rebalancing of load where required. Moreover, contractors often do not require payment until a percentage

[1] This is the total additions in 2008, including customer contributions, less the $400,000 in development contributions

[2] VECC has calculated this amount by using the number $1,526,104 then dividing it by 0.833 or the monthly average spending of $152,610 in 2008 for the first ten months and applying it to the last two months

of the job is completed or when the job is fully complete. According to Midland, VECC has incorrectly equated the flow of spending to when work was performed. Midland objected to VECC's proposed further reduction in 2008 capital spending.

In summary, Midland submitted that if its capital spending is reduced, it will create a backlog of infrastructure projects. Midland submitted that if projects are not completed in a timely manner, system reliability and safety would be at risk. Midland maintained that capital projects in 2008 and 2009 are warranted and that it has been proactive in developing its capital budgets to provide a foundation for the replacement/upgrade to existing infrastructure, other capital requirements and to plan for future development. Midland submitted that its proposed capital budget was consistent with the prudent operation of the distribution system and the engineering report on the substations. Midland concluded that the proposed rate base of $12,202,110 for the 2009 Test Year should be accepted by the Board.

**Board Findings**

The substation renewal program is one of the primary drivers of the capital budget. The Board is satisfied that Midland has conducted that program appropriately in terms of the evaluation of the assets and the timing of the specific projects.

Excluding the impact of the substation renewal program, the capital budget has still increased significantly in percentage terms from the historical period. SEC invited the Board to apply the same approach to Midland as it did to Enbridge Gas Distribution in EB-2005-0001 and reduce the budget to be more in line with historical norms. The Board does not agree that such an approach is appropriate in this case. For such an approach to be appropriate, the Board must be satisfied that the historical level of expenditures is the sustainable level of expenditures. There is limited evidence of such in this case. Indeed it is much more likely that the recent levels of capital expenditure were generally inadequate to ensure the long term health of the system. However, the Board must be mindful of the impact on consumers from sudden and dramatic capital expenditure increases. Such increases must be accomplished in a staged and orderly manner so as to manage the impact on rates. In this case, Midland has provided satisfactory explanations for the significant increases, namely the purchase of a double bucket truck to replace an 18 year vehicle, pole line expansion to meet customer growth and developer expansion payments to comply with the Distribution System Code. The Board has concluded that no reduction to the capital budget is required.

The Board will make no adjustment to the 2008 capital budget for rate base purposes. The Board is satisfied with Midland's explanation that its spending will have been on target for the year.

**Working Capital Allowance**

VECC submitted that the cost of power used to calculate working capital allowance should be updated to reflect the most recent forecast. This was $60.30/MWh as noted in the Board's October 2008 Regulated Price Plan Report. VECC also recommended that since distributors are not billed by the IESO for all components of the RPP price, the Board should work with distributors and the IESO to establish a common approach to determine the elements of the RPP price that should be included in the Cost of Power for purposes of determining working capital allowances. VECC further submitted that working capital allowances should also reflect the most recent estimate of the costs of Hydro One Network's transmission services for 2009.

In Reply, Midland argued that it had used the latest Board approved Hydro One charges to calculate the Transmission Network and Connection charges. Midland agreed to use the rate of $60.30/MWh as suggested by VECC and also updated the Rural Remote Electricity Rate Protection Rate from $0.0010 to $0.0013 in accordance with the Board letter dated December 17, 2008.

SEC expressed concern that the use of a 15% level to determine the working capital allowances significantly overstated the actual working capital requirements of distributors. SEC submitted that in order for the Board to have better information on working capital requirements, Midland should be directed to undertake a lead-lag study and file it with their next rebasing application. SEC noted that other distributors have quoted the costs of such a study being prohibitive and not feasible for a small utility. As an alternative, SEC supported a generic approach to this issue under the auspices of the Board.

Midland rejected SEC's suggestion of a lead-lag study, citing the costs involved, but supported the possibility of a generic study through a consultation process.

**Board Findings**

The Board finds that Midland, in preparing the Draft Rate Order consequential to this Decision, shall use the price of $0.06072/kWh contained in the April 2009 RPP price report, and the latest Board approved Hydro One charges to calculate the Transmission Network and Connection charges.

The Board understands that the IESO does not bill distributors solely on the basis of RPP; however, the Board is satisfied that RPP is a reasonable proxy for purposes of determining the working capital allowance.

The Board concludes that it would not be cost effective for utilities such as Midland to undertake individual lead lag studies, and therefore will not direct Midland to conduct such a study. .

**SMART METERS**

Midland requested a rate rider of $1.00 per customer per month to fund Smart Meter activities. Midland expects to complete installation of all smart meters within its service territory in the 2009 Test Year at an estimated cost of $190 per installed meter. Midland projected the smart metering initiative to cost approximately $1.5 million in 2009.

Midland has confirmed that its Smart Meter Plan does not include costs to support functionality that exceeds the minimum functionality adopted in Ontario Regulation 425/06. Further, Midland has not incurred nor expects to incur any costs associated with functions for which the Smart Metering Entity has the exclusive authority to carry out pursuant to Ontario Regulation 393/07.

VECC in its submission supported Midland’s request for the $1.00 per customer smart meter rate adder.

**Board Findings**

The Board finds that Midland’s proposal is in accordance with the Board Guideline on Smart Meter Funding and Cost Recovery. The Board approves a smart meter funding adder of $1.00 per month per metered customer

## COST OF CAPITAL and CAPITAL STRUCTURE

The Board's policies with respect to capital structure and cost of capital are set out in its *Report on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors*, issued December 20, 2006. Midland submitted that its proposals were consistent with Board policy and appropriately reflected the Board's Cost of Capital Parameter Updates for 2009 Cost of Service Applications issued on February 24, 2009. Midland's proposed capital structure and cost of capital are set out in the following table.

**Midland's proposed capital structure and cost of capital**

| Capital Component | Total Capital Structure (%) | Cost rate (%) |
|---|---|---|
| Long-Term Debt | 52.67 | 4.64 |
| Short-Term Debt | 4.00 | 1.33 |
| Equity | 43.33 | 8.01 |
| Total | 100.00 | |

### Board Findings

The Board accepts Midland's proposed capital structure and cost of capital. The proposal is consistent with Board policy and reflects the updated cost rates established by the Board.

## COST ALLOCATION AND RATE DESIGN

The following issues are addressed in this section:

- Line Losses
- Low Voltage Costs
- Revenue to Cost Ratios
- Retail Transmission Service Rates

### Line Losses

Midland proposed a Distribution Loss Factor ("DLF") of 1.0301 based on the average for the last four of five years. In its submission, Board staff submitted that Midland's proposed DLF of 1.0301 and proposed Total Loss Factor ("TLF") of 1.0651 are consistent with other partially embedded distributors of similar size and profile. SEC agreed the loss factors should be accepted as filed.

**Board Findings**
The Board accepts Midland's proposed loss factors.

**Low Voltage Costs**
In its original filing, Midland requested Low Voltage ("LV") costs of $339,515. These LV charges did not take into account Hydro One's proposed rate changes. Board staff submitted that Midland should assume that Hydro One's proposed sub-transmission rates, to take effect May 1, 2009 (EB-2008-0187), will determine its costs in 2009. Midland replied by updating its forecast on the basis of the May 1, 2009 sub-transmission rates. Midland's updated its forecast LV costs for 2009 to $279,640, and submitted that the Board should approve this new amount.

Staff also submitted that as a future test year cost of service application, Midland is properly allocating LV charges on the basis of 2009 figures. VECC agreed with the proposed allocation of LV costs in its submission.

**Board Findings**
The Board accepts Midland's proposal.

**Revenue to Cost Ratios**
Table 3 sets out Midland's current and proposed revenue-to-cost ratios, as well as proposed ratios of the parties, where applicable. The Board's target ranges, as established in the Board Report, *Application of Cost Allocation for Electricity Distributors* (EB-2007-0667) are set out in column 2. The results of Midland's Cost Allocation informational filing are set out in column 3. Midland proposed the revenue-to-cost ratios set out in column 4.

**Table 3 - Revenue to Cost Ratios**

| 1 Customer Class | 2 Board Target Range[3] | 3 Cost Allocation Informational Filing | 4 2009 Rate Application, as proposed | 5 2009 VECC Alternate ratios[4] | 6 2009 SEC proposed ratios |
|---|---|---|---|---|---|
| | | | | | |
| Residential | 85-115 | 118.18 | 107.00 | 124.58 | 113.50 |
| GS < 50kW | 80-120 | 97.96 | 98.00 | 105.58 | 97.96 |
| GS > 50kW | 80-120 | 83.67 | 98.00 | 69.67 | 83.67 |
| Street Lighting | 70-120 | 23.46 | 49.00 | 25.77 | 46.73 |
| Sentinel Lighting | 70-120 | 28.21 | 49.00 | 31.03 | 49.11 |
| USL | 80-120 | 117.38 . | 100.00 | 120.16 | 114.00 |

Board staff noted in its submission that the proposed ratios across all classes are within the Board's target ranges and that the changes proposed are in line with the Board's policy, insofar as they move the revenue-to-cost ratios closer to unity in all instances, with the noted exceptions of street and sentinel Lighting.

SEC noted the weaknesses of current cost allocation information, but submitted that in general Midland should be moving the revenue-to-cost ratios in all classes towards unity.

On the proposed revenue-to-cost ratios as a whole, VECC submitted that the surplus revenue generated by increasing the revenue-to-cost ratios for street lighting, sentinel lighting, and GS>50 should be used to reduce the revenue-to-

[3] Report of the Board, *Application of Cost Allocation for Electricity Distributors,* November 28, 2007.
[4] VECC IR #6(c). Reflects the removal of transformer allowance from the result at column 3, Midland's Cost Allocation Informational Filing, consistent with Midland's proposal in the application.

cost ratio for Unmetered Scattered Load ("USL") down to 120%, and then be used to move classes above a 100% revenue-to-cost ratio proportionately closer to unity.

VECC expressed concern with two aspects of how Midland's cost allocation ratios were derived: determination of cost responsibility, and transformer ownership allowance.

VECC argued that Midland's use of class revenue requirement distribution from the Cost Allocation Informational filing to determine cost responsibility for 2009 was inappropriate. It noted that billing parameters have changed since that study was performed and that, in some instances, the differences are material. VECC submitted that the reference shares for cost responsibility derived on the basis of 2008 billing parameters, and used in determining revenue-to-cost ratios at VECC IR#6c, should be used as a starting point for determination of changes to cost allocation.

Midland submitted that it would not be appropriate to change the method due to the fact that the alternative method suggested by VECC would need to be fully explored to ensure the process is sound, and that VECC has used different criteria to arrive at a new starting point for the allocation of revenue and costs to customer classes. Midland noted that SEC had submitted that the current cost allocation information is the best available information at this time.

VECC argued that Midland's original cost allocation informational filing improperly assigns the cost of transformer ownership allowance across all classes, resulting in an over allocation of cost to those classes where customers generally do not own their own transformers. VECC submitted that it would be more appropriate to update the informational filing to align with Midland's proposal to assign all transformer ownership allowance costs to the GS>50 classes. VECC's interrogatory #6c shows these revenue-to-cost ratios.

Midland submitted that it would be most appropriate at this time for LDCs to apply a consistent methodology until an alternative has been developed, tested, and approved by the Board. Midland submitted that the Board should approve the Transformer Allowance method used in the Cost Allocation model and the resulting revenue-to-cost ratios for use in the 2009 application, and address the subject through a consultation process before the 2012 cost-of-service applications are filed.

Board staff noted that Midland's proposal was to increase the revenue-to-cost ratio to 70% in both street and sentinel lighting, phased in over a period of three years, as set out below:

**Table 4 - Midland's Proposed Street and Sentinel Lighting Ratios**

| Customer Class | CA Info Filing | 2009 | 2010 IRM | 2011 IRM |
|---|---|---|---|---|
| Street Lighting | 23.46 | 49 | 60 | 70 |
| Sentinel Lighting | 28.21 | 49 | 60 | 70 |

Staff submitted that the phased-in approach for Midland should be similar to that approved in 2008 for other distributors. In other situations similar to Midland's, the Board in its decisions in 2008 directed that the rates be increased to reach the Board's target range in two or three years. Staff submitted that Midland should be required to reach the lower boundary of the Board's target range for street and sentinel lighting in 2010, rather than 2011 as Midland proposed. SEC concurred. SEC further argued that the revenue-to-cost ratios for street and sentinel lighting should be adjusted to move towards unity during the IRM period, and noted that street lighting has been the biggest beneficiary of the historic over-contribution by the residential and general service rate classes. VECC generally agreed with Midland's proposed adjustment to move approximately half way to the bottom end of the Board's target range.

Midland replied that the appropriate treatment for street and sentinel lighting customers should be to phase-in the balance of the movement to the bottom of the target range over more than one year. Midland submitted that the Board should direct Midland to phase-in the movement of the revenue-to-cost ratios for the street lighting and sentinel lighting customer classes over the entire IRM period, which would mitigate the bill impacts.

SEC submitted that as in many other decisions of the Board, the policy should be followed and under-contributing classes should be moved, stepwise, towards the bottom of the range. SEC stressed that classes already within the Board's target ranges should not be altered. SEC claimed that Midland has acted contrary to Board policy by proposing an additional amount of revenue responsibility for the GS>50kW class.

SEC claimed that there is a “perverse” situation in which the GS classes do not get rate relief in the franchise areas where they are over-contributing, but they are forced to give up the benefit of inter-class subsidies in franchise areas in which they are under-contributing, as is the case in Midland.

Similarly, VECC disagreed with the move to unity for USL customers, noting that the USL class is already within the Board’s target range and should not be altered. Midland replied that the USL class has a small number of customers and that revenue allocation is also small. Midland argued that these customers would likely have smart meters installed in 2010, and as a result would move to the GS<50kW class.

VECC submitted that the revenue-to-cost ratio for the GS>50 class should be moved to 80%, subject to the Board’s bill impact criteria. Midland replied that VECC based this ratio on its alternative cost allocation run at VECC IR#6, which used a different starting point. Midland submitted that using VECC’s alternative model would be inappropriate, as noted above.

**Board Findings**

The Board understands VECC’s desire to continue to refine and improve cost allocation. The Board has adopted VECC’s approach to dealing with the transformer ownership allowance in a number of cases, and will do so in this case as well. The Board will not adopt the other revisions proposed by VECC. The Board is satisfied that the revenue to cost ratios derived from the informational filing and adjusted for the transformer ownership allowance provide an adequate starting point at this time.

The Board accepts Midland’s proposal to move the street and sentinel lighting classes half-way to the bottom of the Board’s target range. The Board will require that these classes be moved to 70% with Midland’s 2010 IRM application. The Board understands that there are significant bill impacts involved, but moving these classes to the Board’s range in two years is consistent with a number of other Board decisions in this area.

The Board also agrees that the residential revenue to cost ratio should be reduced. The Board directs that this ratio be reduced to the top of the Board's target range, namely 115%.

The Board also directs that the USL ratio be reduced to the top of the Board's target range, namely 120%.

If the result of these changes is that additional revenue must be recovered, then the Board believes it would be appropriate to raise the ratio for the GS>50 kW class as it is the furthest below 100% and directs Midland to do so.

### Retail Transmission Service Rates

Board staff submitted that Midland's Retail Transmission Service Rates ("RTS rates"), as updated in response to Board Staff interrogatories, account for the update to Hydro One's Uniform Transmission Rates and address the concern regarding growing balances in account 1584 and account 1586. Staff submitted that the RTS rates developed by Midland are designed to collect the associated revenues appropriately. VECC submitted that the RTS rates proposed by Midland should be approved by the Board.

### Board Findings

The Board finds that the RTS rates as proposed by Midland are appropriate.

## DEFERRAL AND VARIANCE ACCOUNTS

The following table sets out the account balances (as of December 31, 2007 with interest forecast to April 30, 2009) which Midland proposed to clear for disposition. Midland did not forecast principal transactions beyond December 31, 2007.

**Deferral and Variance Accounts Requested for disposition by Midland**

| ACCOUNT # | ACCOUNT NAME | BALANCE |
|---|---|---:|
| 1508 | Other Regulatory Assets | $89,068 |
| 1550 | LV Variance Account | $122,180 |
| | Total | $211,248 |

Midland's proposal was to collect these balances over two years via rate riders. Board staff, VECC, and SEC agreed with Midland's proposal to clear accounts 1508 and 1550.

Board staff submitted that the Board may wish to consider disposition of additional accounts in this proceeding. The table from Board staff's submission is reproduced below.

**Deferral and Variance Accounts to be considered for disposition**

| ACCOUNT # | ACCOUNT NAME | BALANCE - $ |
|---|---|---|
| 1508 | Other Regulatory Assets – Sub-Account – OEB Cost Assessments | $15,791 |
| 1508 | Other Regulatory Assets – Sub-Account – Pension Contributions | $73,277 |
| 1518 | Retail Cost Variance Account – Retail | $(8,739) |
| 1550 | Low Voltage Variance Account | $122,180 |
| 1580 | RSVA – Wholesale Market Service Charge | $(395,943) |
| 1582 | RSVA – One-time Wholesale Market Service | $15,930 |
| 1584 | RSVA – Retail Transmission Network Charge | $280,233 |
| 1586 | RSVA – Retail Transmission Connection Charge | $(1,029,880) |
| 1588 | RSVA – Power (including Global Adjustment) | $672,930 |
| | **Total** | **$(254,221)** |

In its reply, Midland agreed with Board staff's proposal to clear the balances in these accounts at this time rather than waiting for the separate initiative related to RSVA and RCVA accounts. Midland also submitted that the accounts should be recovered by way of a variable rate rider over the four year rebasing period, in order to smooth rates for customers. Midland proposed a recovery period of two years in its original application.

No party proposed that the accounts related to smart meters, PILs or Regulatory Asset Balances should be disposed of at this time.

**Board Findings**

The Board finds that all of the accounts in the table above should be disposed of at this time. The Board notes that Midland agrees with this approach. In keeping with Midland's original proposal, the Board finds that this net credit balance should be returned to customers over two years. The Board finds that there is no benefit to customers of extending the disposition to four years as proposed by Midland.

**IMPLEMENTATION**

The Board has made findings in this Decision which change the 2009 distribution rates from those proposed by Midland. These changes are to be reflected in a Draft Rate Order prepared by Midland.

The Board issued an Interim Rate Order on April 30, 2009 making Midland's current rates interim, which allows for an effective date of May 1, 2009. As Midland was not late in filing its application, the Board has determined that an effective date as of May 1, 2009 is appropriate. As a result there will be a period of time starting on May 1, 2009 that Midland will have charged customers according to its currently approved rates rather than the Board approved 2009 rates. In order to recover this foregone distribution revenue the Board will allow Midland to, in its rate order, provide for a rate rider or rate riders and their start and end dates, that will enable Midland to recover any difference in revenue.

Based on this Decision the Board directs Midland to file the proposed rate rider(s), the duration of the proposed rate rider(s), the supporting materials to justify the rate rider(s) and to satisfy the Board that the revenues received would adequately recover the foregone revenues.

In filing its Draft Rate Order, it is the Board's expectation that Midland will not use a calculation of the revised revenue deficiency to reconcile the new distribution rates with the Board's findings in this Decision. Rather, the Board expects Midland to file detailed supporting material, including all relevant calculations showing the impact of this Decision on Midland's proposed revenue requirement, the allocation of the approved revenue requirement to the classes and the determination of the final rates. Supporting documentation shall include, but not be limited to, filing a completed version of the Revenue Requirement Work Form excel spreadsheet, which can be found on the Board's website. Midland should also show detailed calculations of the revised low voltage rate adders, retail transmission service rates and variance account rate riders reflecting this Decision

**RATE ORDER**

A Rate Order decision will be issued after the processes set out below are completed.

**COST AWARDS**

The Board may grant cost awards to eligible stakeholders pursuant to its power under section 30 of the *Ontario Energy Board Act, 1998*. When determining the amount of the cost awards, the Board will apply the principles set out in section 5 of the Board's Practice Direction on Cost Awards. The maximum hourly rates set out in the Board's Cost Awards Tariff will also be applied.

All filings with the Board must quote the file number EB-2008-0236**,** and be made through the Board's web portal at www.errr.oeb.gov.on.ca, and consist of two paper copies and one electronic copy in searchable / unrestricted PDF format. Filings must be received by the Board by 4:45 p.m. on the stated date. Please use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at www.oeb.gov.on.ca. If the web portal is not available you may e-mail your documents to the attention of the Board Secretary at BoardSec@oeb.gov.on.ca. All other filings not filed via the Board's web portal should be filed in accordance with the Board's Practice Directions on Cost Awards.

**THE BOARD DIRECTS THAT:**

1. Midland shall file with the Board, and shall also forward to Intervenors, a Draft Rate Order attaching a proposed Tariff of Rates and Charges reflecting the Board's findings in this Decision, within 14 days of the date of this Decision. The Draft Rate Order shall also include customer rate impacts and detailed supporting information showing the calculation of the final rates.

2. Intervenors shall file any comments on the Draft Rate Order with the Board and forward to Midland within 7 days of the filing of the Draft Rate Order.

3. Midland shall file with the Board and forward to Intervenors responses to any comments on its Draft Rate Order within 7 days of the receipt of any submissions.

4. Intervenors shall file with the Board and forward to Midland their respective cost claims within 26 days from the date of this Decision.

5. Midland shall file with the Board and forward to the relevant Intervenor any objections to the claimed costs within 40 days from the date of this Decision.

6. The relevant intervenor shall file with the Board and forward to Midland any response to any objections for cost claims within 47 days of the date of this Decision.

7. Midland shall pay the Board's costs incidental to this proceeding upon receipt of the Board's invoice.

**DATED** at Toronto, May 12, 2009
**ONTARIO ENERGY BOARD**

*Original signed by*

Kirsten Walli
Board Secretary