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**Susan Frank**

Vice President and Chief Regulatory Officer  
Regulatory Affairs

May 17, 2010

BY COURIER

Ms. Kirsten Walli  
Secretary  
Ontario Energy Board  
2300 Yonge Street  
Suite 2700,  
Toronto, ON.  
M4P 1E4

Dear Ms. Walli:

**EB-2010-0060 – OEB Consultation on Distribution Revenue Decoupling -  
Hydro One Networks' Comments**

Attached are three (3) paper copies of Hydro One Networks' comments on Distribution Revenue Decoupling and the Pacific Economics Group Research report that was issued on March 22, 2010.

I have also attached proof of successful submission of these comments through the Board's Regulatory Electronic Submission System.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank

**HYDRO ONE COMMENTS  
ON BOARD STAFF DISCUSSION PAPER:  
REVIEW OF DISTRIBUTION REVENUE DECOUPLING MECHANISMS**

Hydro One Networks (“Hydro One”) is pleased to provide comments on the issues identified by the Ontario Energy Board (“the Board”) staff and the Pacific Economics Group Research (“PEG”) report dated March 19, 2010, titled “*Review of Distribution Revenue Decoupling Mechanisms.*”

This submission consists of two sections:

1. Introduction and General Comments
2. Responses to Board Staff’s Issues for Comment

**1. INTRODUCTION AND GENERAL COMMENTS**

The Board has initiated a consultation process to examine the revenue adjustment and cost recovery mechanisms that are currently available to electricity and natural gas distributors to address revenue erosion resulting from unforecasted changes in the volume of energy sold.

The Board retained PEG to analyze the mechanisms currently available to Local Distribution Companies (“LDCs”) against selected alternative approaches used in different jurisdictions. These include Lost Revenue Adjustment Mechanisms (“LRAMs”), Partial and Full Decoupling True-Up Plans and Straight Fixed Variable Pricing (“SFV”).

Hydro One does not believe that additional revenue decoupling is required at this time for its distribution or transmission businesses and that robust and accurate load forecasting and regular cost of service hearings are a more appropriate means for dealing with the revenue impacts associated with load changes over time. Hydro One believes that the following points support this position:

- SFV plans, although simple to implement, could penalize low use customers and benefit high use customers by increasing the fixed component of a customer’s bill. This outcome does not support the government’s policy of moving towards a culture of conservation.
- True up plans can lead to retroactive rate making. Variances due to revenue changes accumulate in accounts for future disposition and can lead to rate volatility. After the fact changes can also lead to revenue recognition issues for external reporting, an issue of particular concern to distributors that are also public securities issuers and reporting filers.
- Hydro One supports CDM and the targets set by the OPA. Hydro One believes that a forward test-year approach combined with an appropriate load forecast that

takes into account all CDM impacts, including LDC and other entity programs as well as customer-initiated actions, adequately addresses the issue of revenue erosion.

- As recently noted by the Board, Hydro One has a sophisticated load forecasting methodology that anticipates demand changes. As a result, Hydro One has not experienced and does not expect to experience significant unanticipated revenue erosion.
- Operating efficiency and productivity is supported by regular rate hearings where costs and revenues are reviewed and challenged in detail.
- Although LRAMs are complex to implement and Hydro One has concerns with validating and measuring CDM achievements, such mechanisms are currently available to Ontario LDCs.

Revenue decoupling mechanisms are not a factor for rates set under cost of service. The flexibility to submit regular cost of service applications must be maintained in the future. Revenue decoupling may need to be considered for LDCs that are under a multi year Incentive Regulation (“IR”) plan where there is the potential for load reduction to lead to revenue erosion.

Also, LDCs within Ontario are operating under different circumstances. Each is undertaking different levels and types of CDM initiatives that make sense for its customer base. Some are experiencing significant customer load growth while others are not or may in fact be experiencing declines in customer base. Each has its own particular needs for modifying and expanding its systems to accommodate renewable generation. Some are required to invest significantly in aging infrastructure while others have relatively new systems. Certain revenue decoupling mechanisms may or may not make sense depending on the circumstances that an LDC faces. As a result, flexibility is required in the application of revenue decoupling mechanisms and their implementation should be at the option of the LDC.

## **2. RESPONSES TO BOARD STAFF’S ISSUES FOR COMMENT**

- 1. In light of developments in metering, CDM and demand side management (“DSM”), among possible others, is the implementation of further or modified revenue decoupling mechanisms for electricity and/or gas distributors warranted at this time and if so, why? For example, is the Board’s current Lost Revenue Adjustment Mechanism adequate in light of the contemplated introduction of CDM targets for all electricity distributors in the Province?*

Yes, there is a need to modify the LRAM mechanism for LDCs that are under multi-year IR plans. The current LRAM process is complex and controversial. A more simplified and formulaic approach is required that would define how the savings will be measured at the outset of the implementation of a CDM program. For example, a refrigerator

replacement program would identify the savings associated with each refrigerator replaced and this would be applied to the number of units replaced to determine the load decrease. If this were achieved, the LRAM approach should be sufficient to address revenue erosion attributable to CDM for LDCs under multi year IR plans.

**2. *What factors should be considered when assessing the suitability of Ontario's current mechanisms and of alternative approaches? Are any of these factors more or less important than others? If so, why?***

The following factors should be considered when assessing the suitability of Ontario's current mechanisms and the alternative approaches:

- **Flexibility** – Any approach needs to be flexible in its application. As noted above, LDCs in Ontario operate under very different circumstances. Revenue decoupling mechanisms may or may not make sense depending on the circumstances that an LDC faces. As a result, flexibility is required in the application of revenue decoupling mechanisms.
- **Fairness** – Any approach needs to be fair and equitable for electricity consumers. SFV and Partial and Full Decoupling True-Up Plans that are applied evenly to all customers within a class could penalize low usage customers within that class and unfairly benefit high use customers.
- **Support of CDM Targets** – Revenue decoupling mechanisms should not detract from the Province's direction on energy conservation and the attainment of CDM targets. Mechanisms that increase the fixed component of customer rates reduce the benefit that customers can achieve when reducing electricity consumption and could negatively impact the attainment of CDM targets. Hydro One has made a significant investment in smart meters to support time of use pricing and conservation that are expected to be instrumental in achieving conservation targets.
- **Simplicity** – Revenue decoupling should not be overly complex to implement and administer. Historically, LRAMs have a high associated cost and administrative burden due to their reliance on having to estimate CDM/DSM savings. These savings can be complex and controversial to validate and measure. SFV pricing, on the other hand, would be relatively simple to administer. It is important to note that the introduction of Revenue Decoupling mechanisms would not reduce Hydro One's requirements for robust load forecasting as this is still required for business planning.
- **Comprehensiveness** – If revenue decoupling is pursued it should be comprehensive in nature. LRAMs do not take into account programs that are carried out by the Ontario Power Authority (such as improved building codes and efficiency standards) or other entities (such as federal and provincial tax incentives). They typically only take into account the programs administered by the LDC. Therefore, the current LRAM does not capture the true CDM-driven load reduction.

Hydro One believes that of the factors noted above, flexibility is particularly important due to the different circumstances faced by Ontario LDCs.

***3. What, if any, are the implications of the wide-spread deployment of smart meters for the Board's approach to revenue decoupling?***

Hydro One, like other LDCs in Ontario, has made significant investments in smart meters. Decoupling mechanisms that increase the fixed component of a customer's bill could send the wrong message to customers and negatively impact conservation. Approximately 30% of a typical Hydro One residential customer's distribution bill would be fixed with the implementation of SFV pricing.

***4. What scope for further or modified revenue decoupling might be appropriate? For example, should the impact of all variances from forecast in commodity demand be eliminated regardless of the cause (i.e., distributor-provided CDM/DSM programs, other CDM/DSM programs, the economy, weather, customer growth, etc.)? Why or why not?***

Hydro One's view is that further or modified revenue decoupling is not warranted. If the Board decided to provide an option for LDC's to decouple, the impact should be limited to variances associated with conservation.

***5. Are there any alternative approaches, beyond those identified in the PEG Report, which better address revenue erosion due to changes in consumption? What are the costs, benefits and implications of implementing the alternative approach?***

Hydro One is not aware of other alternative approaches beyond those identified in the PEG Report.

***6. Is there a preferred approach (or elements of an approach) and if so, what are the important implementation matters that must be considered? What are the costs, benefits and implications of implementing the preferred approach or of refraining from doing so?***

For Hydro One's circumstances, the best alternative to address revenue erosion due to changes in consumption is regular cost of service hearings using forward test years.

For LDCs that are under multi-year IR plans, the price cap formula could be modified to address the issue of revenue erosion related to CDM. The current price cap index could be redesigned to incorporate a conservation factor. This conservation factor could take into account the target for the forecast year and prior year actual experience.

***7. Can or should the preferred approach need to be the same in both the gas sector and the electricity sector? Why or why not? Would any other form of differentiation based, for example, on a specific distributor characteristic(s) be appropriate? If so, what might be the defining characteristic(s)?***

The gas and electricity sectors are at very different points when it comes to conservation. The characteristics of LDCs within Ontario are different. Defining characteristics include the rate of customer growth, the age of assets and the level of investment required to maintain reliability and accommodate renewable generation, the commitment to CDM/DSM programs established for customers, the number of CDM/DSM programs and the impact of these programs on average use, customer density and the mix of customers served.

It is difficult to identify a preferred approach based on specific distributor characteristics as these may change over time.