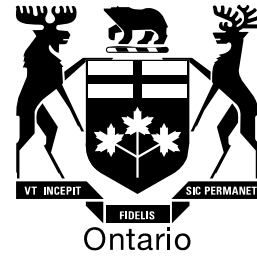


Ontario Energy Board

Commission de l'énergie de l'Ontario



# **Chapter 3 of the Filing Requirements for Transmission and Distribution Applications**

**June 22, 2011**

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# Chapter 3      Filing Requirements for Incentive Regulation Mechanism Rate Applications

## 1.0            Introduction

The Ontario Energy Board establishes the rates of electricity distributors using a combination of annual incentive regulation mechanism (“IRM”) adjustments and periodic cost of service reviews.

The examination of and decision on an application is based only on the evidence filed in that case. This ensures that all interested parties to the proceeding have an opportunity to see the evidence, participate meaningfully in the Board’s process in any given case and understand the reasons for a decision. Consequently, the applicant must, at a minimum, meet all of the applicable Filing Requirements.

The Filing Requirements herein replace version 2.0 of Chapter 3 of the *Filing Requirements for Transmission and Distribution Applications*, dated July 8, 2010. The requirements set out the Board’s expectations for filings by electricity distributors that are applying for annual rate adjustments under an IRM plan.

In its October 27, 2010 letter regarding the development of a Renewed Regulatory Framework for Electricity (“RRF”), the Board announced that it was extending the 3<sup>rd</sup> Generation IRM (“IRM3”) plan until such time as three RRF policy initiatives have been substantially completed. As such, the four-year rate-setting cycle (i.e. rebasing plus three years of IRM) remains in place for the time being. Electricity distributors that have completed a cost of service application for the 2008 rate year and beyond must file an IRM3.

Distributors whose rates have not been rebased since the 2006 EDR are expected to file a cost of service rate application for 2012. In the event that one or more of those distributors elect to remain on an IRM plan and the Board approves such a request, distributors shall file an IRM3 application. The Board has determined that a uniform

IRM framework will allow for greater consistency amongst distributors. Efficiency will also be gained by no longer having to review and maintain different filing modules, especially since the vast majority of distributors have already rebased since the 2006 EDR. Therefore, the Board will no longer allow distributors to file a 2<sup>nd</sup> Generation IRM application.

## 1.1 Key References

The documents listed below are key to understanding these Filing Requirements:

- *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation Mechanism for Ontario's Electricity Distributors* (filing guidelines: Appendix F) – December 20, 2006;
- *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities*, December 11, 2009
- *Guidelines for Electricity Distributors' Conservation and Demand Management* – March 28, 2008 (and any subsequent updates);
- *Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors*– July 14, 2008;
- *Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors* – September 17, 2008;
- *Addendum to the Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors* – January 28, 2009;
- *Guideline (G-2008-0001) on Retail Transmission Service Rates* – October 22, 2008 (Revision 3.0 June 22, 2011 and any subsequent updates);
- *Guideline (G-2008-0002) on Smart Meter Funding and Cost Recovery* – October 22, 2008 (and any subsequent updates);
- *Report of the Board on Electricity Distributors' Deferral and Variance Account Review Initiative (EDDVAR)* – July 31, 2009;
- *Filing Requirements: Distribution System Plans – Filing under Deemed Conditions of Licence* EB-2009-0397 - March 25, 2010;
- *Report of the Board on Transition to International Financial Reporting Standards* EB-2008-0408 – July 28, 2009; and
- *Addendum to Report of the Board EB-2008-0408 – Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment* – June 13, 2011

## 1.2 Grouping for Filings

The Board will assign electricity distributors in one of six application groupings noted below based on the expected level of complexity of the application.

The length of time required to review an application is commensurate upon its level of complexity. Applications of greater complexity and hence requiring more time to review will be required to be filed first. Staggering of the applications allows the Board and other stakeholders to appropriately schedule resources to allow for adequate review of the applications. The deadlines for filing an IRM application have been determined so that, in the normal course of events, a Decision and Order would be issued in time for a May 1 implementation date.

The application deadlines are as follows:

- Friday September 16, 2011
- Friday September 30, 2011
- Friday October 14, 2011
- Friday October 28, 2011
- Friday November 10, 2011
- Friday November 25, 2011

For those distributors whose rate year has been aligned with their fiscal year, the application deadline for a January 1, 2012 implementation date will be August 15, 2011.

Board staff will survey potential IRM applicants in June 2011 requesting that applicants identify the expected elements of their IRM application for the purpose of assisting the Board in assigning a filing deadline for each electricity distributor. Applicants expected to include one or more of the following elements in their application will be assigned an earlier filing date:

- LRAM/SSM recovery;
- Revenue-to-Cost Ratio Adjustments pursuant to a prior Board decision;

- Rate Harmonization pursuant to a prior Board decision;
- Z Factor claim;
- Incremental Capital Module claim; and
- Renewable Generation and/or Smart Grid Rate Adder request.

The assignment of distributors under these filing dates will be identified in a separate communication.



### 1.3 Components of the Application Filing

Each application must include:

- A Manager's Summary thoroughly documenting and explaining all rate adjustments applied for;
- The contact information for the IRM application - The primary contact for the IRM application may be a person within the applicant's organization other than the primary licence contact. The Board will communicate with this person during the course of the application. After completion of the IRM application, the Board will revert communication to the primary licence contact;
- A completed Rate Generator<sup>1</sup> and supplementary work forms<sup>2</sup>, provided by the Board, both in electronic (i.e. Excel) and PDF form;
- A PDF copy of the current Tariff Sheet;
- Supporting documentation cited within the application (e.g. excerpt of relevant past decision, relevant Reporting and Record-keeping Requirements ("RRR") data and Revenue Requirement Work Form ("RRWF"))<sup>3</sup>; and
- Statement as to which publication(s) the applicant's notice will be appearing, whether it is a paid publication or not and the readership and circulation numbers.

### 1.4 Bill Impacts

The Rate Generator includes a bill impact analysis by rate class and produces total bill impacts excluding any changes to the Regulated Price Plan ("RPP"). This analysis is similar to that used in assessing rate applications in recent years. The latest RPP at the time of publication of the Rate Generator model will be used and will remain unchanged for the duration of the application process.

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<sup>1</sup> The Rate Generator is a Microsoft Excel workbook that calculates a distributor's proposed tariff of rates and charges in an IRM Application.

<sup>2</sup> Include the Shared Tax Savings Workform, Revenue Cost Ratio Adjustment Workform, Incremental Capital Module Workform, Deferral and Variance Account Workform and RTSR Adjustment Workform.

<sup>3</sup> The Revenue Requirement Work Form is filed as part of the draft rate order in the last rebasing application.

## **1.5 Applications and Electronic Models**

The models prepared by Board staff are provided to assist the distributor in filing a rate application. An application to the Board is the distributor's responsibility and the Board expects that the application will be complete and accurate. While Board staff may issue electronic filing models for use in IRM rate applications, the distributor bears the responsibility to ensure the accuracy and appropriateness of any models that it uses in supporting its application. The distributor is responsible for advising the Board of any concerns it may have regarding calculations flowing from the models. Utilization of Board staff models does not necessarily constitute Board acceptance.

## **1.6 Other Rate Adjustments**

The Rate Generator will be made available on the Board's web site. The model will include generic base rate adjustments, rate adders and rate riders common to most applicants. Where a distributor has continuing adjustments, and/or rate adders and/or rate riders from previous decisions that are not in the generic model (such as the phased implementation of a rate harmonization process) the distributor should contact Board staff for specific guidance.

## **2.0 Elements of the IRM Plan**

### **2.1 Price Cap Index Adjustment**

The Gross Domestic Product Implicit Price Index for Final Domestic Demand (GDP-IPI) as published by Statistics Canada for the prior calendar year will be used as the price escalator for IRM applications with rates effective May 1, 2012. Board staff's models will originally include the preceding year's GDP-IPI value as an estimate of the inflationary adjustment to input prices (i.e. costs) for the upcoming rate year. Statistics Canada publishes the prior year's data at the end of February. Upon publication by Statistics Canada, the Board will issue a letter establishing the updated GDP-IPI. Board staff will update the GDP-IPI in each distributor's rate application model in order to calculate the price cap index adjustment for distribution rates for all applicants.

For those distributors whose rate year has been aligned with their fiscal year, the annual percentage change in the GDP-IPI for the period 2010 Q3 to 2011 Q2 to 2009 Q3 to 2010 Q2 will be used in the final rate application model.

The price cap index adjustment is determined as the annual percentage change in the GDP-IPI less the X-Factor. The X-factor is 0.72% plus a stretch factor. The value of the stretch factor is specific to each distributor for each rate year, and will be one of the following values: 0.2%; 0.4%; or 0.6%. The Board will determine each distributor's stretch factor. The distributor specific stretch factors will not be available before the application is filed. Therefore, the IRM model will include a proxy stretch factor of 0.4%. Once the distributor specific stretch factors become available, the Board will adjust the stretch factor in each distributor's individual rate application model.

The price cap index adjustment will not be applied to the following components of delivery rates:

- Rate Adders;
- Rate Riders;
- Low Voltage Service Charges;
- Retail Transmission Service Rates;
- Wholesale Market Service Rate;
- Rural Rate Protection Charge;
- Standard Supply Service – Administrative Charge;
- MicroFIT Service Charge;
- Specific Service Charges; and
- Transformation and Primary Metering Allowances.<sup>4</sup>

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<sup>4</sup> and any other allowances the Board may determine.

## 2.2 Incremental Capital Module

The incremental capital module (“ICM”) is intended to address the treatment of new capital investment needs that arise during the IRM plan term which are incremental to the materiality threshold defined below.

The eligibility criteria to recover amounts that are incremental to capital investment needs are included in section 2.5 of the *Report of the Board on 3<sup>rd</sup> Generation Incentive Regulation for Ontario’s Electricity Distributors*, dated July 14, 2008 and are reproduced below.

Criteria	Description
Materiality	The amounts must exceed the Board-defined materiality threshold and clearly have a significant influence on the operation of the distributor; otherwise they should be dealt with at rebasing.
Need	Amounts should be directly related to the claimed driver, which must be clearly non-discretionary. The amounts must be clearly outside of the base upon which rates were derived.
Prudence	The amounts to be incurred must be prudent. This means that the distributor’s decision to incur the amounts must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.

### 2.2.1 ICM Materiality Threshold

The ICM materiality threshold is discussed in section 2.3 of the *Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario’s Electricity Distributors* (the “Supplemental Report”) EB-2007-0673.

The Board has determined that the following formula is to be used by a distributor to calculate the materiality threshold that will apply to it:

$$\text{Threshold Value} = 1 + \left(\frac{\text{RB}}{\text{d}}\right) * (\text{g} + \text{PCI} * (1 + \text{g})) + 20\%$$

Where:

- RB = rate base included in base rates (\$);
- d = depreciation expense included in base rates (\$);
- g = distribution revenue change from load growth (%); and
- PCI = price cap index (% inflation less productivity factor less stretch factor).

The values for "RB" and "d" are the Board-approved amounts in the distributor's base year rate decision.

The value for "g" is the % difference in distribution revenues between the most current complete year and the base year.

The following table provides an example of the calculation of the materiality threshold values.

<b>An Illustration:</b>	
Assumptions:	RB = \$100 million; d = \$5 million; g = 1.5% (0.015); and PCI = 0.75% (0.0075).
Calculation:	$1 + \left(\frac{100,000,000}{5,000,000}\right) * (0.015 + .0075 * (1 + 0.015)) + 0.20 = 1.65$
Result:	The materiality threshold (CAPEX/Depreciation) is 1.65 or 165%. That is, given the assumptions in this example, the Board expects the distributor to manage a CAPEX level of up to \$8.26 million (\$5 million * 1.65) before being eligible to apply to recover incremental amounts.

### 2.2.2 Eligible Incremental Capital Amount

In the Supplemental Report, the Board determined that eligible incremental capital amount sought for recovery should be new capital in excess of the materiality threshold. The threshold values, as calculated using the threshold formula discussed in Section 2.2.1, establishes a threshold that determines eligibility for incremental capital spending but also marks the base from which to calculate the maximum amount eligible for

recovery. A distributor applying for recovery of incremental capital should calculate the eligible incremental capital amount by taking the difference between the 2012 total non-discretionary capital expenditure and the materiality threshold.

### **2.2.3 Application of the Half-Year Rule**

The Board's general guidance on the application of the half-year rule is provided in the Supplemental Report. In this report the Board determined that the half-year rule should not apply so as not build a deficiency for the subsequent years of the IRM plan term. In a subsequent decision with respect to the application of the half-year rule in the context of an ICM, the Board clarified that the half-year rule would apply in the final year of the IRM plan term<sup>5</sup>.

### **2.2.4 Revenue Requirement Calculation**

When calculating the revenue requirement associated with the ICM, a distributor should use the following parameters:

- Cost of Capital
  - In the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors*, issued December 20, 2006 ("2006 Report") the Board outlined the transition to a single deemed capital structure of 60% debt and 40% equity. Since all distributors have completed the transition to a 60/40 debt-equity ratio, a distributor filing for an ICM adjustment shall use this deemed capital structure.
  - On December 11, 2009 the Board issued the *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities* (the "2009 Report"). The 2009 Report sets out revised cost of capital parameters to be effected in cost of service applications. A distributor filing an ICM adjustment, shall use the last Board-approved cost of capital parameters determined during the distributors last rebasing application

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<sup>5</sup> EB-2010-0130, Guelph Hydro Electric Systems Inc., *Decision and Order*, p. 15

when calculating the revenue requirement associated with the ICM.

- PILS
  - Since currently known legislated tax changes from the level reflected in the Board-approved base rates for a distributor will be reflected in the IRM adjustments, a distributor filing for an ICM adjustment should apply the current tax rates when calculating the revenue requirement associated with the ICM.

### **2.2.5 ICM Filing Guidelines**

The Board requires that a distributor requesting relief for incremental capital during the IRM3 plan term must include comprehensive evidence to support the claimed need, which should include the following:

- Details by project for the proposed capital spending plan for the test year segregated between discretionary and non-discretionary;
- Demonstration that the distributor's non-discretionary spending exceeds the threshold test;
- A description of the proposed non-discretionary capital projects and expected in-service dates;
- Demonstration that the proposed non-discretionary capital projects are unusual and unanticipated;
- Calculation of the revenue requirement associated with each proposed incremental non-discretionary capital project (i.e. the cost of capital, depreciation, and PILs);
- Calculation of revenue requirement offsets associated with each incremental non-discretionary projects due to revenue to be generated through other means (e.g. customer contributions in aid of construction); and
- Calculation of a rate rider to recover the incremental revenue from each class and the rationale for the proposed approach.

## **2.2.6 ICM Reporting Requirements**

A distributor that receives rate relief through this module will be required to report to the Board annually on the actual amounts spent. At the time of the next rebasing, the distributor will file a calculation of the amounts to be incorporated in rate base. At that time the Board will make a determination on the treatment of any difference between forecast and actual capital spending during the IRM plan term. Any overspending or underspending will be reviewed at the time of rebasing.

## **2.2.7 ICM Accounting Treatment**

The distributor will record eligible ICM amounts in Account 1508, Other Regulatory Asset, sub-account Incremental Capital Expenditures, subject to the assets being used and useful. For incremental capital assets under construction, the normal accounting treatment will continue in the construction work in progress (“CWIP”) prior to these assets going into service and hence eligible for recording in the 1508 sub-account. The amortization of capital assets for the relevant accounting period will be recorded in a separate amortization account of the sub-account, Incremental Capital Expenditures. In addition, the revenues collected from the rate rider will be recorded in Account 1508, Other Regulatory Asset, sub-account, Incremental Capital Expenditures rate rider.

The distributor shall also record monthly carrying charges in sub-accounts Incremental Capital Expenditures and Incremental Capital Expenditures rate rider. Carrying charges amounts are calculated using simple interest applied to the monthly opening balances in the account and recorded in a separate sub-account of account 1508. The rate of interest shall be the rate prescribed by the Board for deferral and variance accounts for the respective quarterly period published in the Board’s web site.

## **2.2.8 Rate Generator and Supplemental Filing Module for ICM**

The supplemental filing module supporting Board staff’s IRM3 Rate Generator will assist the distributor in calculating the distributor’s threshold. The distributor will then tabulate the value of its eligible non-discretionary investments and compare this to the threshold.



Other calculation work forms will be provided to calculate the revenue requirement for each project proposed for inclusion in the ICM request in the supplemental filing module. Once all work forms are completed and listed in the supplemental module, the tabulated revenue requirement will be converted into a rate rider.

## 2.3 Z-factor Claims

Z-factors are intended to provide for unforeseen events outside of a distributor’s management control. The cost to a distributor must be material and its causation clear. A distributor must follow the guidelines listed below when applying to the Board to recover the amounts that the distributor has recorded in a Board-approved deferral account related to a Z-factor claim.

### 2.3.1 Eligibility Criteria for Z-factor Amounts

The eligibility criteria for a request to recover amounts by way of a Z-factor are discussed in section 2.6 of the *Board’s Report on 3<sup>rd</sup> Generation Incentive Regulation for Ontario’s Electricity Distributors* – July 14, 2008, and are summarized in Table 1 below. In order for amounts to be considered for recovery by way of a Z-factor, the amounts must satisfy all three eligibility criteria set out in Table 1 below.

**Table 1: Z-factor Amount Eligibility Criteria**

Criteria	Description
Causation	Amounts should be directly related to the Z-factor event. The amount must be clearly outside of the base upon which rates were derived.
Materiality	The amounts must exceed the Board-defined materiality threshold and have a significant influence on the operation of the distributor; otherwise they should be expensed in the normal course and addressed through organizational productivity improvements.
Prudence	The amount must have been prudently incurred. This means that the distributor’s decision to incur the amount

	must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.
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### 2.3.2 Materiality Threshold

The following materiality thresholds will apply:

- \$50,000 for a distributor with a distribution revenue requirement less than or equal to \$10 million;
- 0.5% of distribution revenue requirement for a distributor with a revenue requirement greater than \$10 million and less than or equal to \$200 million; and
- \$1 million for a distributor with a distribution revenue requirement of more than \$200 million.

The materiality threshold must be met on an individual event basis in order for the relevant costs to be eligible for potential recovery.

### 2.3.3 Z-factor Filing Guidelines

A distributor must submit evidence that the costs incurred meet the three eligibility criteria outlined above. A distributor must also:

- Notify the Board by letter to the Board Secretary of all Z-factor events. Failure to notify the Board within six months of the event may result in disallowance of the claim.
- Apply to the Board for any cost recovery of amounts recorded in the Board-approved deferral account claimed under Z-factor treatment. This will allow the Board and any affected distributor the flexibility to address extraordinary events in a timely manner. Subsequently, the Board may review and prospectively adjust the amounts for which Z-factor treatment is claimed.
- The Board requires that any request for a Z-factor will be accompanied by a clear demonstration that the management of the distributor could not have been able

- The costs must be incremental to those already being recovered in rates as part of ongoing business exposure risk.

#### **2.3.4 Other Matters in Relation to Z-Factors**

As part of its claim, a distributor must outline the manner in which it intends to allocate the incremental revenue requirement to the various customer rate classes, the rationale for the selected approach and a discussion of the merits of alternative allocation methods. Recovery will be through a rate rider<sup>6</sup>. The request must specify whether the rate rider(s) will apply on a fixed or variable basis or a combination thereof, and the length of the disposition period and a rationale for this proposal. A detailed calculation of the rate rider(s) must be provided.

#### **2.3.5 Z-factor Accounting Treatment**

The distributor will record eligible Z-factor cost amounts in Account 1572, Extraordinary Event Costs, of the Board's Uniform System of Accounts (the "USoA") contained in the *Accounting Procedures Handbook* ("APH") for electricity distributors. Monthly carrying charges shall be recorded in Account 1572. Carrying charges are calculated using simple interest applied to the monthly opening balances in the account and recorded in a separate sub-account of this account. The rate of interest shall be the rate prescribed by the Board for deferral and variance accounts for the respective quarterly period published on the Board's web site.

### **2.4 Off-ramps**

An off-ramp is based on a pre-defined set of conditions under which the IRM plan would be terminated or modified before its normal end-of-term date due to excessive over or under earnings.

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<sup>6</sup> See Appendix C

For IRM3, the Board determined that the plan will include a trigger mechanism with an annual ROE dead band of  $\pm 300$  basis points. When a distributor performs outside of this earnings dead band, a regulatory review may be initiated. As such, a distributor will be required to report to the Board no later than 60 days after the company's receipt of its annual audited financial statements, in the event that the distributor's earnings falls short of or exceeds its ROE by 300 basis points. A review will be carried out by the Board to determine if further action by the Board is warranted. Any such review would be prospective in nature, and could result in modifications to the IRM3 plan, a termination of the IRM3 plan or the continuation of the IRM3 plan for that distributor.

## **2.5 Tax Changes**

Under an IRM3, a 50/50 sharing<sup>7</sup> of the impact of currently known legislated tax changes as applied to the tax level reflected in the Board-approved base rates for a distributor applies. The calculated annual tax changes over the plan term will be allocated to customer rate classes on the basis of the most recent Board-approved base-year distribution revenue. These amounts will be collected from or refunded to customers each year of the plan term, over a 12-month period, through an explicit volumetric rate rider derived using annualized consumption by customer class underlying the Board-approved base rates.

A shared tax saving workform will include a schedule for a distributor to complete, which will calculate the volumetric rate rider. Occasionally, the calculated rate adders or rate riders for one or more rate classes may be negligible. In the event that the calculation of one or more rate classes' rate rider results in energy-based kWh rate riders of \$(0.0000) when rounded to the fourth decimal place and demand-based kW rate riders of \$(0.00) when rounded to the second decimal place, or is negligible, the distributor may apply to record the amount to be recovered or refunded in USoA account 1595 disposition in a future rate setting.

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<sup>7</sup> Supplemental Report of the Board on 3rd generation incentive regulation – September 17, 2008

## 3.0 Implementation Matters

### 3.1 Deferral and Variance Account Balances

The *Report of the Board on Electricity Distributors' Deferral and Variance Account Review Report* (the "EDDVAR Report") provides that during the IRM plan term, the distributor's Group 1 audited account balances will be reviewed and disposed if the preset disposition threshold of \$0.001 per kWh (debit or credit) is exceeded. The onus is on the distributor to justify why any account balance in excess of the threshold should not be disposed.

Group 1 consist of the following USoA accounts:

- 1550 Low Voltage Account;
- 1580 RSVA Wholesale Market Service Charge Account;
- 1584 RSVA Retail Transmission Network Charges Account;
- 1586 RSVA Retail Transmission Connection Charge Account;
- 1588 RSVA Power (Including Global Adj. Sub a/c) Account;
- 1590 Recovery of Regulatory Asset Balances Account; and
- 1595 Disposition and Recovery of Regulatory Balances Account.

The EDDVAR Report states that the default disposition period to clear the Group 1 account balances by means of a rate rider should be one year. However, a distributor could propose a different disposition period to mitigate rate impacts or address any other applicable considerations, where appropriate.

Subsequent to the release of the EDDVAR Report, exogenous events resulted in significant increased balances in the USoA Account 1588 global adjustment sub-account for most electricity distributors. The global adjustment sub-account captures the difference between the amounts billed (or estimated to be billed) to non-RPP customers by the distributor and the actual amount paid by the distributor to the IESO.

During the 2010 and 2011 EDR process, the Board determined in most cases that a separate rate rider included in the delivery component of the bill would apply prospectively to non-RPP customers to dispose of the global adjustment sub-account balances.

### **3.1.1 Special Purpose Charge (“SPC”)**

The Board authorized Account 1521, Special Purpose Charge Assessment Variance Account in accordance with Section 8 of Ontario Regulation 66/10 (Assessments for Ministry of Energy and Infrastructure Conservation and Renewable Energy Program Costs) (the “SPC Regulation”). Accordingly, any difference between (a) the amount remitted to the Minister of Finance for the distributor’s SPC assessment; and (b) the amounts recovered from customers on account of the assessment must be recorded in “Sub-account 2010 SPC Assessment Variance” of Account 1521.

In accordance with Section 8 of the SPC Regulation, distributors and are required to apply no later than April 15, 2012 for an order authorizing the disposition of any residual balance in sub-account 2010 SPC Assessment Variance.

The Board expects that requests for disposition of the balance in “Sub-account 2010 SPC Assessment Variance” and associated carrying charges will be addressed as part of the proceedings to set rates for the 2012 rate year. Exceptions may apply in cases where this approach would result in non-compliance with the timeline set out in section 8 of the SPC Regulation.

### **3.2 Revenue-to-Cost Ratio Adjustments**

The Board’s Decisions for some distributors’ 2008, 2009, 2010 and 2011 cost of service rate applications prescribed a phase-in period to adjust the revenue-to-cost ratios. The Supplemental Filing Module and Rate Generator will include schedules for a distributor to effect revenue-to-cost ratio adjustments previously approved by the Board. The process will adjust base distribution rates before the application of the price cap adjustment.

### **3.3 Electricity Distribution Retail Transmission Service Rates**

Electricity distributors are charged the Ontario Uniform Transmission Rates (“UTRs”) at the wholesale level and subsequently pass these charges on to their distribution customers through the Retail Transmission Service Rates (“RTSRs”). The UTRs are charges for network, line connection and transformation connection services.

Distributors shall adjust their RTSRs based on a comparison of historical transmission costs adjusted for new UTR levels and revenues generated from existing RTSRs. This approach will minimize variances in USoA Account 1584 and 1586. A filing module prepared by Board staff will be provided to distributors at the time of the release of the Rate Generator to assist in calculating the distributor’s and rate class specific RTSRs. The filing module will reflect the most recent Uniform Transmission Rates approved by the Board (EB-2010-0002), issued on January 18, 2011 and effective January 1, 2011. Once the January 1, 2012 UTR adjustments are determined, the Board will adjust each distributor’s 2012 IRM rate application model to incorporate this change, if applicable. This approach reflects the revised Guideline for *Electricity Distribution Retail Transmission Service Rates*, dated June 22, 2011.

### **3.4 Lost Revenue Adjustment Mechanism (LRAM) and/or Shared Savings Mechanism (SSM) Cost Claims**

As noted in the Board’s CDM Guidelines (EB-2008-0037) unforecasted CDM results can have the effect of eroding distribution revenues due to lower than forecast throughput. The lost revenue adjustment mechanism (“LRAM”) is a retrospective adjustment, which is designed to account for differences between the forecast revenue loss embedded in rates and the actual revenue loss.

While the LRAM removes the disincentive to delivery CDM Programs, a shareholder incentive, the shared savings mechanism (“SSM”), is also available to encourage distributors to pursue cost effective CDM programs. The SSM is available for CDM programs funded through distribution rates.

### **3.4.1 Input Assumptions**

When calculating LRAM, the Board has stated in recent decisions that at the time of the third party review of CDM Programs, the most current Ontario Power Authority (“OPA”) Measures and Assumptions lists, as updated by the OPA from time to time, represent the best estimate of losses associated with a distributor’s CDM programs and should be used by distributors. The Board has also accepted finalized program evaluations delivered to distributors from the OPA in relation to OPA programs that the distributor has implemented as long as the distributor has included relevant documentation from the OPA in its application.

### **3.4.2 Deadline for filing LRAM and SSM applications**

The Board has approved LRAM and SSM applications for many distributors since the beginning of the Third Tranche CDM period in 2005. It is the Board’s understanding that there may still be remaining distributors who have yet to apply to the Board for recovery of LRAM and/or SSM amounts related to CDM activities undertaken between 2005 and 2010.

Distributors intending to file an LRAM or SSM application for CDM Programs funded through distribution rates, or an LRAM application for CDM Programs funded by the OPA between 2005 and 2010, shall do so as part of their 2012 rate application filings, either cost-of-service or IRM. If a distributor does not file for the recovery of LRAM or SSM amounts in its 2012 rate application, it will forego the opportunity to recover LRAM or SSM for this legacy period of CDM activity.

### **3.5 Smart Meter Funding Adder**

In 2008 the Board issued Guidelines (G-2008-0002) (“Smart Meter Guideline”) pertaining to smart meter funding and cost recovery. These guidelines provisioned for a smart meter funding adder<sup>8</sup>, as well as two variance accounts for distributors to record smart meter expenditures and revenues collected through the smart meter funding adder.

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<sup>8</sup> See Appendix C



The smart meter funding adder was designed as a tool to provide advance funding and to mitigate the anticipated rate impact of smart meter costs when recovery of those costs are approved by the Board. As of May 2011, 4.6 million or 98% of meters have been installed province-wide. With deployment nearing completion, the Board stated in previous decisions that it expects distributors to file for a final prudence review at the earliest possible opportunity following the availability of audited costs. The Board also approved a sunset date of April 30, 2012 for the smart meter funding adder for most distributors in their 2011 rate application.

Smart meter capital and operating costs will affect a distributor's rate base and revenue requirement. Under the existing IRM framework, there is no re-evaluation of rate base or of the revenue requirement for the purpose of setting distribution rates. A distributor seeking a prudence review of smart meter costs during the IRM plan term shall file a separate smart meter cost recovery application. A distributor filing a stand-alone smart meter cost recovery application must comply with the Smart Meter Guideline or any further updates to it.

### **3.6 Distribution System Plans - Filing under Deemed Conditions of Licence**

The *Filing Requirements: Distribution System Plans - Filing under Deemed Conditions of Licence* (EB-2009-0397) issued on March 25, 2010 recognized that distributors may need additional funding for expenditures proposed in a GEA Plan between cost-of-service applications. For 2012 IRM applications, distributors may request the following:

- Renewable Generation Connection Funding Adder; and
- Smart Grid Funding Adder.

Where a distributor seeks a funding adder, sufficient information must be provided to allow the Board to assess the need for the mechanism and the nature and quantum of the costs to be collected from ratepayers and the basis for calculating the funding adder. The costs recovered through the funding adder will be subject to a prudence review in the first cost of service application following the implementation of the funding

adder. A refund to ratepayers may be ordered if the Board find that the expenditures upon which the adder was based were not prudently incurred.

In the Distribution System Plan Filing Requirements, the Board created two additional deferral accounts to record the amounts collected from ratepayers through the funding adders:

- Account 1533: Renewable Generation Connection Funding Adder Deferral Account

This account will record the revenues collected through a funding adder approved by the Board related to renewable generation connection projects. Separate sub-accounts shall be used to record any amounts collected from a distributor's ratepayers and any amounts received from the IESO (pursuant to the provincial pooling mechanism set out in 79.1 of the OEB Act) in respect of the projects.

- Account 1536: Smart Grid Funding Adder Deferral Account

This account will record the revenue collected through a funding adder approved by the Board related to smart grid development.

### **3.7 Transition to International Financial Reporting Standards ("IFRS")**

The Board provided general guidance on this topic in the *Report of the Board, Transition to IFRS*, issued on July 28, 2009 and in associated amendments available on the IFRS page of the Board's website (amendments are dated November 8, 2010 and March 15, 2011).

On June 13, 2011 an *Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment* (EB-2008-0408) (the "Addendum") was issued following a working group process. The Addendum sets out additional regulatory policy regarding the transition to IFRS in the circumstance where utilities rates are rebased using cost of service rate setting methods and where rates are subsequently set using an incentive rate-setting mechanism. For distributors

that rebased under CGAAP and are filing an IRM application issues 1 and 2 in the Addendum are of particular relevance.

## **4.0 Specific Exclusions from IRM Applications**

The IRM application process is intended to streamline the processing of a large volume of rate adjustment applications, and is therefore mechanistic in nature. For this reason, the Board has determined that the IRM process is not the appropriate venue by which a distributor should seek relief on issues which are substantially unique to an individual distributor or more complicated and potentially contentious. The following are examples of specific exclusions from the IRM rate application process:

- Prudence Review of Smart Meter Cost;
- Rate Harmonization, other than that pursuant to a prior Board decision;
- Changes to revenue-to-cost ratios, other than pursuant to a prior Board decision;
- Loss Factor Changes;
- Loss Carry Forward Adjustments to PILs/taxes; and
- Loss of Customer Load.

Exclusions from the IRM process are to be addressed in the distributor's next cost of service application with the exception of distributors seeking a prudence review of smart meter costs which should be addressed in a separate (or stand alone) application.

## **Appendix A: Disposition of Residual Balance in USoA Account 1590 or 1595**

The 2006 Regulatory Assets process disposed of all balances in the regulatory asset accounts as of December 31, 2004. The decisions for each distributor resulted in the disposition of the approved amounts by way of final rate riders and the transfer of the approved amounts to account 1590. Likewise, any deferral and variance account balances post December 31, 2004 that have been approved by the Board for disposition were disposed on a final basis, unless otherwise noted and should have been transferred to account 1595.

Accounts 1590 and 1595 are part of the Group 1 deferral and variance accounts as defined by the Board in the EDDVAR Report. Once the rate rider ceases, the residual principal balances and any interest carrying charges in these accounts would be cleared in an IRM application (where applicable) provided that the preset disposition threshold for the Group 1 accounts has been exceeded.

## **Appendix B: Application of Recoveries to Principal and Interest Carrying Charges Amounts in Account 1595**

When final approval for disposition of deferral and variance account balances is received from the Board, the final approved amounts of principal and interest carrying charges is transferred to account 1595.

The cumulative principal balance transferred to account 1595 is drawn down by the rate rider recoveries, and interest carrying charges are applied to the principal balance net of recoveries.

The following approach is used for the application of recoveries (via rate riders) to the transferred amounts under two scenarios:

### **Scenario 1: Rate Rider ceases with Principal amount remaining**

If the rate rider ends before the principal is fully drawn down, the principal balance is held static and interest carrying charges are applied to the remaining principal balance. The approved rate rider flowing from the next application to dispose of deferral and variance accounts should include the remaining principal and interest carrying charges.

### **Scenario 2: Rate Rider ceases with no Principal amount remaining but with Interest Carrying Charges remaining**

The approved rate rider flowing from the next application to dispose of deferral and variance account balances should include the cumulative interest carrying charge amounts.

## **Appendix C: Rate Adder versus Rate Rider**

### **Rate Adder**

A rate adder (or funding adder) is a tool designed to provide advance funding on an interim basis to distributors for certain investments or expenses as prescribed by the Board and to mitigate or smooth the anticipated rate impact when recovery of these costs are approved by the Board. Approval of a rate adder does not constitute regulatory approval of any costs actually incurred. The prudence of such costs is examined, and the costs are approved in whole or in part, at the time at which the distributor brings the matter forward for regulatory review.

Rate adders are identified and listed separately on a distributor's Tariff of Rates and Charges.

### **Rate Rider**

A rate rider differs from a rate adder in that it is designed to recover or refund Board-approved amounts following a prudence review. Rate riders are identified and listed separately on a distributor's Tariff of Rates and Charges, with an explicit sunset or termination date.

### **Materiality for Rate Adders and Rate Riders**

Rate adders and rate riders normally apply to one or more select rate classes on a fixed basis, a volumetric basis or a combination of both. A rate adder or rate rider is usually determined by dividing the Board-approved allocated amounts by the Board-approved forecast or historical energy use or demand.

Occasionally, the calculated rate adders or rate riders for one or more rate classes may be negligible. In the event where the calculation of one or more rate classes' rate adder or rate rider results in energy-based kWh rate riders of \$(0.0000) when rounded to the fourth decimal place and demand-based kW rate riders of \$(0.00) when rounded to the second decimal place, or are negligible, the entire Board-approved amount for recovery

or refund shall be recorded in a USoA account to be determined by the Board for disposition in a future rate setting.