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3 **REPLY ARGUMENT**

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5 **1.0 A SUMMARY OF THE PROPOSED RATE APPLICATION**

6 On November 15, 2005, Hydro One Networks Inc. (“Hydro One” or “the Company”)
7 applied on behalf of its Distribution business for Ontario Energy Board (“Board”)
8 approval of rates applicable to eligible current and new generator customers in the
9 General Service – Three Phase and Sub-Transmission classes of its core customers and
10 the General Service class of acquired customers. Requirements for eligibility are a three-
11 phase connection to Hydro One’s distribution system and interval metering in place.
12 These rates are proposed for implementation on an interim basis until Hydro One’s cost
13 allocation review is complete and resulting new rates applicable to these customers may
14 be approved for implementation. Today such generators are charged the appropriate
15 monthly service charge regardless of volumetric use. This Application proposes that the
16 current distribution rates for these eligible generator customers be amended to permit
17 charging them the distribution volumetric rate only. Hydro One has requested permission
18 to establish a deferral account to track the estimated \$160,000 annual reduction in
19 distribution revenues due to this proposal and the one-time set-up costs of \$25,000, until
20 they may be addressed in the next rate proceeding. If this Application is approved,
21 Hydro One would require five weeks to build the new rates into the billing system,
22 followed by another four weeks to migrate all the eligible customers to the new rates.

23 **2.0 A SUMMARY OF INTERVENOR ARGUMENTS**

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25 Five intervenors – Schools Energy Coalition (“SEC”), Vulnerable Energy Consumers
26 Coalition (“VECC”), Energy Cost Management Inc. (“ECMI”), the Association of Power
27 Producers of Ontario (“APPrO”) and Mr. Glen Estill of Sky Generation Inc. (“Sky
28 Generation”) – submitted arguments. All arguments support distributed generation in the
29 Province. SEC and VECC do not support this Application, whereas ECMI, APPrO and
30 Mr. Estill do support it. The following sections summarize the individual submissions.

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2.1 Schools Energy Coalition

SEC does not support Hydro One’s Application, stating that Hydro One provides no evidence of a financial barrier to distributed generators, nor any analysis to support the complete removal of the service charge. Furthermore, no generator affected by this Application filed evidence of such disincentives. SEC indicates that savings due to the Company’s proposal are small vis-à-vis the potential capital investment required to establish such an operation. It asks the Board to deny this Application for the reasons above, and also for the reason that approval of this rate would be unfair to other rate classes. It suggests taking this issue to the Board’s cost allocation process underway.

2.2 Vulnerable Energy Consumers Coalition

VECC believes that Hydro One’s proposal is an inappropriate response to the need for new generation in the Province and asks that approval be denied, due to:

- a) the slight extent to which the temporary financial relief provided by this rate change would affect the long-term investment decisions of potential distributed generators.
- b) the potential inequitable treatment of rate classes, should the Board depart from the principle of cost causality on behalf of one rate class, but then return to it for others. (Other customers could argue financial hardship in support of reduced rates.)
- c) the precedent which would be set by accepting the argument for financial hardship. Distributed generators can be expected to use this argument again if, through the cost allocation process, their rates are increased, and when deferred costs related to this filing are proposed for recovery in rates.
- d) the inconsistency of this proposal with the Board’s Decision on the 2006 EDR Process, which decided against making changes to either customer classes or to the design of rates, pending the outcome of its cost allocation review.

VECC states that other consumers will subsidize these rates and if such cross-subsidies are to be implemented, this should be the result of explicit Government policy (to be paid

1 for by all consumers) and not the creation of one local distribution utility. VECC
2 believes that the Ontario Power Authority's procurement process is the best mechanism
3 to achieve this result.

4 5 **2.3 Energy Cost Management Inc.**

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7 ECMI agrees with Hydro One's stated intent to reduce some of the disincentive with
8 respect to connection of distributed generators. It believes that the cost-based
9 compromise raised during the 2006 EDR process would have been beneficial, leaving
10 end-use customers financially indifferent. Despite finding the lack of cost justification
11 "somewhat unsettling," ECMI generally supports Hydro One's proposal.

12 13 **2.4 Association of Power Producers of Ontario**

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15 APPrO supports Hydro One's proposal. APPrO also agrees with Hydro One's plan to
16 establish a rate class and distributed generator rates following a cost allocation review. It
17 would welcome more predictable rate-making and would not support an approach that
18 would raise rates and/or institute a more complicated rate-making process. APPrO notes
19 several benefits of distributed generators – reduction of distribution line losses, the
20 potential to defer or avoid capital upgrade expenditures, increased distribution system
21 reliability and the provision of support and/or ancillary services. It would like the
22 upcoming allocation of costs to distributed generators to reflect the total network benefits
23 they provide and also only those costs that can reasonably be considered necessary to
24 provide distribution service to distributed generators.

25 26 **2.5 Sky Generation Inc.**

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28 Mr. Estill of Sky Generation discusses the same benefits of distributed generation as
29 those noted by APPrO. He states that, due to price adjustments made by distributors on
30 the rare occasions when distributed generators increase line losses, these generators will

1 never increase consumer costs, but will nearly always reduce them. For these reasons, he
2 states that distributed generators offer system benefits for which they are not paid. He
3 not only supports Hydro One's proposal, but requests retroactive application to the time
4 in 2004 when discussions on this issue began. Mr. Estill argues that this approach would
5 not set a broad precedent, as there are not many requests for change which also offer
6 ratepayers a reduction in overall costs. He believes that distributors should treat
7 generation customers differently from load customers, for the reason that generators,
8 similarly to transmission and distribution systems, are built to serve load customers. Mr.
9 Estill asserts it is therefore appropriate for the cost of transmission and distribution
10 systems to be largely borne by load customers, with such costs to be borne by generation
11 customers only in proportion to their use of electricity.

12 13 **3.0 HYDRO ONE'S RESPONSES TO INTERVENOR ARGUMENTS**

14 15 **3.1 SEC and VECC**

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17 SEC and VECC make similar arguments with respect to the low level of relief provided
18 by Hydro One's proposal and the potential inequity it may pose for other rate classes. In
19 response to the first issue, Hydro One submits that the savings resulting from these
20 proposed rate changes may seem small, but can nonetheless be critical for a small start-up
21 operation. Mr. Estill's letter on behalf of Sky Generation supports this point, by noting
22 its potential annual savings of about \$3,000 as a result of this proposal. It also notes the
23 benefits of this proposal vis-à-vis leaving in place "punitive charges that discourage the
24 installation of distributed generation."

25
26 The Company recognizes the potential precedent-setting nature of the argument of
27 financial hardship, noted by VECC. In order to mitigate this concern, the Company has
28 proposed the implementation of these rate changes for only an interim period until the
29 cost allocation review is complete and newly resulting rates may be implemented.

1 **3.2 ECMI**

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3 ECMI generally agrees with Hydro One's proposal. Hydro One believes that the issue
4 raised by ECMI's argument was addressed during the 2006 EDR process.

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6 **3.3 Sky Generation Inc. and APPrO**

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8 Hydro One believes that a greater number of distributed generators will assist the
9 Province with its goal of increasing the sources of clean, reliable electricity generation.
10 The Company also believes that the benefits of distributed generation as listed by Mr.
11 Estill and APPrO are directionally correct. Hydro One, however, is unable to accept the
12 analyses and calculations underlying a number of Mr. Estill's statements. For example,
13 distributors apply metering adjustments to purchased power depending on the location of
14 the meter vis-à-vis the generator, which is necessary to provide fair and equitable
15 treatment to all customers. Mr. Estill's assumptions on this issue led to his conclusion
16 that "distributed generation in Ontario will never result in an increase in electricity costs
17 for consumers [due to line losses], and will in almost all cases, result in a decrease in
18 consumer costs" -- one of the "system benefits for which they are not paid."

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20 In response, Hydro One would like to clarify that not all distributed generators are
21 equally beneficial to the distribution system in all the ways espoused. Many of the
22 benefits of distributed generation are related to the commodity only. The value of the
23 benefits they provide to the distribution system will depend on the types of generators,
24 the complexity of their connections, their locations on the system and the applicable loss
25 factors, among other variables. Accordingly, these stated benefits, if they can be properly
26 quantified, should be considered along with the total cost of investment, in the
27 examination of demand and supply which is being undertaken as part of the Ontario
28 Power Authority's standard offer program.

1 APPrO is concerned that the upcoming cost allocation review could result in a rate
2 increase for distributed generators which in its view, would be unjustified. Hydro One
3 cannot guarantee that the rates for distributed generators will not increase as a result of
4 the upcoming cost allocation review, but can consider measures (such as phasing-in the
5 implementation of a potential increase) to help address this issue.

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7 With respect to retroactive application, Hydro One submits that the purpose of this
8 proposal, as stated in response to Interrogatory E-1-2, is to help encourage new
9 generation until the cost allocation review is complete and the resulting rates for
10 distributed generation customers are approved. As discussed in more detail in response
11 to this Interrogatory, Hydro One's billing system cannot handle retroactive rate
12 adjustments. For these reasons and in view of the Board's previous disallowance of a
13 retroactive approach, again as stated in response to this Interrogatory, Hydro One does
14 not support any retroactive application of these proposed rates.

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16 Hydro One agrees with Mr. Estill's statement that transmission and distribution system
17 costs should be borne by load and generation customers in proportion to their use of
18 electricity.

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20 **4.0 CONCLUSIONS**

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22 Hydro One continues to submit that its proposal is a reasonable interim approach to assist
23 the Provincial Government in encouraging the growth of distributed generation in the
24 Province. Mr. Estill has reinforced the Company's assumption that the savings proposed
25 by the removal of the service charge are important to a small start-up operation. Hydro
26 One believes that any potential issues which may be raised by other customers are
27 addressed through the request to make this an interim measure until cost allocation results
28 may be implemented.

1 As a result of having made this Application, Hydro One has become aware of
2 misunderstandings regarding the treatment of costs and benefits of distributed generation.
3 The upcoming cost allocation review may assist in clarifying those aspects which are
4 related to the distribution system.