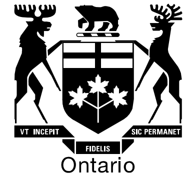
Ontario Energy Board

Commission de l'énergie de l'Ontario



EB-2010-0132

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 Hydro One Brampton Networks Inc. for an order approving or fixing just and reasonable rates and other charges for the distribution of electricity to be effective January 1, 2011.

BEFORE: Paula Conboy
Presiding Member

Cathy Spoel
Member

DECISION AND ORDER

BACKGROUND

Hydro One Brampton Networks Inc. ("HOBNI" or the "Applicant") filed an application with the Ontario Energy Board (the "Board") on June 30, 2010. The application was filed under section 78 of the *Ontario Energy Board Act, 1998*, S.O 1998, c. 15 (Schedule B) (the "Act"), seeking approval for changes to the rates that it charges for electricity distribution to be effective January 1, 2011. HOBNI is the licensed electricity distributor serving approximately 131,000 customers in the City of Brampton.

HOBNI is one of 80 electricity distributors in Ontario whose rates are regulated by the Board. 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, as amended on June 28, 2010, outlines the filing requirements for cost of service rate applications, based on a forward test year, by electricity distributors.

On March 5, 2009, the Board informed HOBNI that it would be one of the electricity distributors to have its rates rebased for the 2011 rate year. This was confirmed in the Board's letter of April 20, 2010. Accordingly, HOBNI filed a cost of service application based on 2011 as the forward test year.

The Board assigned the application file number EB-2010-0132 and issued a Notice of Application and Hearing dated July 22, 2010. The Board approved four interventions: the Energy Probe Research Foundation ("Energy Probe"); the School Energy Coalition ("SEC"); and the Vulnerable Energy Consumers Coalition ("VECC"). PowerStream Inc. sought and was granted intervenor status, but did not participate actively in the proceeding. No letters of comment were received by the Board.

In Procedural Order No.1 issued on August 26, 2010, the Board established a schedule for the delivery of interrogatories and responses, a technical conference and a settlement conference.

In Procedural Order No.2 issued on October 8, 2010, the Board made provision for parties to provide submissions on the response to an interrogatory for which HOBNI requested confidential treatment.

The technical conference was conducted on October 13, 2010. Undertakings arising from the technical conference were filed on October 18, 2010. The settlement conference was held on October 19, 2010 and no settlement was reached on any of the issues.

On November 3, 2010, the Board issued its Decision on Confidentiality and Procedural Order No.3 establishing dates for parties to provide submissions on further procedural steps in this proceeding and, in particular, on which issues should be addressed through written submissions and which, if any, should be considered as part of an oral hearing.

In Procedural Order No.4 issued on November 17, 2010, the Board established dates for an oral hearing to allow parties to clarify specific issues in this proceeding. The oral hearing was convened on December 6 and 7, 2010.

On December 13, 2010, the Board issued its Procedural Order No.5 establishing the process for Argument-in-Chief ("AIC") and written final submissions. HOBNI's reply submission was filed on January 26, 2011.

HOBNI originally requested a revenue requirement of $66,581,754[1] to be recovered in new rates effective January 1, 2011. The application indicated that the existing rates would produce a revenue deficiency of $4,042,406 for 2011. The resulting requested rate increase was estimated as 9.8% on the delivery component of the bill for a residential customer consuming 800 kWh per month. A GS<50 kW customer consuming 2,000 kWh per month would experience a 2.1% decrease in their delivery charge.

HOBNI filed updates to its application on September 2, 2010. HOBNI amended its application as a result of its decision to defer its transition to International Financial Reporting Standards ("IFRS"). The revenue requirement was restated on the basis of the Canadian Generally Accepted Accounting Principles ("CGAAP") previously used by the Applicant and the service revenue requirement was adjusted to $62,721,985.

In response to a Board staff interrogatory filed on October 1, 2010, HOBNI provided a breakdown of its revenue requirement confirming further changes between the time it

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[1] This amount did not include Other Distribution Revenue of $3,986,412.

filed the original application and the closing of the interrogatory stage of this hearing. Its updated revenue requirement was $63,068,857.

On November 8, 2010, HOBNI filed another update to its application regarding provincial sales tax cost-savings adjustment, an additional OM&A amount resulting from Low Income Energy Assistance Program ("LEAP"), and an adjustment for Green Energy Act capital expenditures. HOBNI's revenue requirement was adjusted to $62,847,561.

In its AIC, HOBNI stated that the revenue requirement of $62,847,561 reflected adjustments primarily to rate base and operating expenses. The updated proposed rates are set to recover a revenue deficiency of $116,379. These adjustments do not reflect the update to the cost of capital parameters issued by the Board on November 15, 2010 for rates effective January 1, 2011. The Board notes that with the updated cost of capital parameters, the application (as amended at the close of the record) results in an overall revenue sufficiency.

THE ISSUES

Board staff, Energy Probe, SEC and VECC made submissions on the following issues, which are addressed in this Decision:

- Operating Revenue;
- Operating, Maintenance & Administrative Expenses;
- Payments in Lieu of Taxes;
- Rate Base and Capital Expenditures;
- Cost of Capital;
- Cost Allocation and Rate Design;
- Deferral and Variance Accounts;
- Smart Meters;
- LRAM & SSM; and
- Implementation.

OPERATING REVENUE

The following issues are addressed in this section:

- Load Forecast
- Customer Forecast
- Other Distribution Revenue

Load Forecast

HOBNI's load forecast was developed in four steps. First, the Applicant developed a multivariate regression analysis of monthly wholesale purchases for the distribution system from 2001 to 2009. Second, an adjustment was applied to account for the impact of CDM programs. Third, the forecast was adjusted for losses to produce a weather-normalized forecast using average weather conditions over this period. Fourth, forecast total use for each customer class was developed using customer count forecasts and then adjusting these forecasts based on relative weather sensitivity of each class so that the sum of the individual class forecasts equaled the total billed kWh forecasts developed in the first three steps.

HOBNI's proposed load forecast for 2011 is as follows:

Load Forecast

Rate Classes	GWh
Residential	1,107.8
GS<50 kW	290.7
GS 50 to 699 kW	1,123.8
GS 700 to 4999 kW (Intermediate)	832.1
Large User	383.3
Unmetered Scattered Load	4.9
Street Lighting	29.8
TOTAL	**3,772.3**

In general, parties accepted the methodology proposed by HOBNI with the exception of the following: CDM adjustment, GDP growth rate, the conversion to kW for the applicable classes and weather normalization.

<u>CDM adjustment</u>
In its application, HOBNI included a CDM adjustment of 64 GWh in the 2011 load forecast.

Energy Probe argued that the estimate of the CDM adjustment was out of date and too large for the 2011 test year. In the Board's recent Decision on LDC CDM targets (EB-2010-0215/EB-2010-0216) dated November 12, 2010, the Board specified that the 2011-2014 CDM cumulative target for HOBNI is 189.54 GWh. Energy Probe submitted

that the appropriate CDM target to be included in the load forecast for 2011 is 19 GWh, representing 10% of its cumulative target. Energy Probe's position was that since the Board's target is a four year cumulative target, the target or savings achieved in one year are expected to persist in subsequent years. Incremental savings in each of the 2011 through 2014 years would achieve 100% of the target. SEC took the same position.

VECC stated that based on the source data provided by Hydro Ottawa in its 2011 cost of service rate application (EB-2010-0133), the LDC aggregate CDM target value for 2011 is 577 GWh. HOBNI's share is 3.15% of the provincial total which is 18.2 GWh. VECC submitted that this is the appropriate CDM adjustment to be included in 2011.

Board staff submitted that since HOBNI filed its CDM Strategy and Application for Board-Approved CDM Programs which indicates the energy savings for 2011 is 38.8 GWh, the CDM adjustment should reflect this amount. Board staff also suggested that a true-up mechanism would address any revenue deficiency or sufficiency over the IRM period resulting from the implementation of this CDM adjustment.

VECC also expressed its concern over the 64 GWh CDM adjustment made by HOBNI which included CDM savings from Codes and Standards and other parties' programs as well as from the CDM target assigned to HOBNI. VECC stated that the regression model developed by HOBNI should capture not only historical savings but would carry forward into projections for future year trends in the historical data regarding increased CDM savings over time. VECC submitted that it is not appropriate to adjust CDM savings which have already been derived from the model for all anticipated CDM savings in 2011. VECC concluded that it is appropriate to adjust CDM savings for new efforts that would arise from the CDM targets.

In its reply submission, HOBNI confirmed that the 64 GWh adjustment incorporated CDM savings from OPA-contracted and Board approved CDM programs, which included other CDM impacts resulting from various codes and standards as well as federal and provincial government programs. HOBNI further argued that neither Board staff's nor VECC's proposed CDM reductions represented an all-inclusive CDM impact. The Applicant noted that VECC utilized numbers provided by Hydro Ottawa, which are not publicly tested, nor officially provided by the OPA; therefore it submitted that it would be inappropriate to adopt 18.2 GWh as its CDM adjustment.

GDP growth rate

Energy Probe stated that the load forecast is calculated based on a number of variables including a GDP growth rate. In response to Energy Probe interrogatory # 19, HOBNI provided the 2010 and 2011 Ontario GDP growth rates from major Canadian financial institutions. Since the most recent GDP growth rates were provided in interrogatory responses, Energy Probe submitted that the update of the GDP growth rates to more current data is appropriate. VECC concurred. Energy Probe estimated that using the updated GDP would impact the distribution revenue by $190,000 based on the current approved distribution rates.

In its reply submission, HOBNI submitted that it is inappropriate to select data from varying points in time to alter a previously accepted forecasting methodology.

kW load forecast

Energy Probe noted that HOBNI used the exponentially smoothed historical ratio of kW/kWh to calculate the kW billing determinants. Energy Probe submitted that this methodology should be rejected. Energy Probe argued that HOBNI had not provided evidence to support its position that this methodology is more accurate than the simple average of the ratios which has been previously approved by the Board in cost of service applications. Energy Probe submitted that using the exponentially smoothing approach would provide $46,366 more revenue than the simple average approach. Energy Probe concluded that using the simple average ratios is more appropriate.

2011 kW load forecast

kW	GS 50 to 699 kW	Intermediate	Large User	Street Lighting
HOBNI	3,079,920	1,879,169	697,451	88,637
Energy Probe	3,071,351	1,896,247	698,259	88,582

In its reply submission, HOBNI disagreed with Energy Probe. HOBNI argued that its methodology emphasized more recent trends in the relationship between kWh and kW, and that it provided a more accurate forecast than using simple average ratios.

Weather Normalization

HOBNI's normalized weather forecast is based on a 30-year average of monthly Heating Degree Days (HDD) and Cooling Degree Days (CDD). Energy Probe noted that Toronto Hydro Electric Systems Limited and Burlington Hydro had used shorter periods, 10 years and 13 years respectively, to calculate the average. Energy Probe

submitted that the use of the 30 year period was not justified. A shorter period would more accurately reflect recent weather trends. Energy Probe estimated that using the 30-year average monthly HDD and CDD would increase distribution revenue by $125,000. Board staff submitted that HOBNI's methodology was reasonable.

In its reply submission, HOBNI argued that the use of the 30-year average is appropriate and pointed out that Board staff supported the reasonableness of this approach.

BOARD FINDINGS

The Board notes that HOBNI's use of a multivariate regression model to perform its load forecast was generally acceptable to all the parties with the exception of the CDM adjustment, GDP growth rate, the conversion to kW for the applicable classes and weather normalization.

The Board finds that the appropriate CDM adjustment to be included in the load forecast for 2011 is 19 GWh, which represents 10% of its cumulative CDM target for the period of 2011- 2014. The Board is of the view that CDM targets will be achieved on an incremental, staged basis and that any adjustment to the test year's rates should be commensurate with the quantum of forecast savings for the test year. The Board is also inclined to defer imputing a larger impact arising from CDM initiatives into the test year load forecast until a true-up mechanism has been developed. The Board therefore agrees with Board staff's observation that a true-up mechanism is likely required to address any revenue deficiency or sufficiency over the IRM period resulting from the implementation of CDM programs intended to achieve HOBNI's cumulative target. However, the Board will not establish a true-up mechanism at this time as this is a generic issue that is likely to be applicable to all rate regulated distributors and should be determined in that context.

The Board notes that HOBNI argued that its proposed CDM adjustment should include other CDM impacts resulting from various codes and standards and federal and provincial government programs. However, the Board agrees with VECC's argument that the regression model developed by HOBNI captures the projections for future year trends regarding increased CDM savings over time. Therefore there is no need for further adjustments.

In regards to the adjustment related to the GDP growth rate, the Board is of the view that an updated forecast is not required unless there is likely to be a material impact on the revenue deficiency/sufficiency. The Board finds that the change proposed by Energy Probe is not material. The Board accepts the Applicant's proposed GDP growth rates.

The Boards also finds that the change relating to the conversion to kWs and weather normalization that Energy Probe has proposed is not material. The Board therefore accepts the Applicant's proposal.

Customer Forecast

HOBNI's test year customer forecast is 176,675 customers/connections (including Unmetered Scattered Load and Street Lighting connections). The forecast was derived by applying the class specific average growth rates for the exponentially smoothed 2009 data as the growth rate for the bridge and test years. The exponential smoothing technique applies exponentially increasing weighting to more recent data. HOBNI submitted that the use of this methodology recognizes the fact that while HOBNI has seen historically high levels of customer growth the rate of growth has been decreasing in recent years.

Customer Forecast

Rate Classes	2005	2006	2007	2008	2009	2010	2011
Residential	104,822	109,778	117,119	119,060	121,041	122,377	123,660
GS<50 kW	6,892	7,075	7,294	7,437	7,529	7,728	7,893
GS 50 to 699 kW	1,364	1,402	1,417	1,491	1,554	1,544	1,552
Intermediate	121	119	117	116	114	110	106
Large User	3	4	5	6	6	6	6
Unmetered Scattered Load (connections)	1,159	1,207	1,250	1,267	1,280	1,287	1,300
Street Lighting (connections)	32,938	34,321	35,762	37,265	38,829	40,459	42,158
TOTAL	**147,299**	**153,906**	**162,964**	**166,642**	**170,353**	**173,511**	**176,675**
% change		**4.5**	**5.9**	**2.3**	**2.2**	**1.8**	**1.8**

Board staff noted that HOBNI's customer forecast represented a 1.8% annual average growth from 2009 to 2011. Board staff also indicated that the average annual customer

growth experienced during the 2005 to 2009 period was 3.7% and the lowest annual customer growth for that period was 2.2% in 2009.

Board staff questioned the use of such low growth rate assumptions to set rates for the next four years given that the City of Brampton's planning report stated that the period between 2008 and 2011 marked the bottom of the current decline in housing starts.

VECC also expressed a number of concerns regarding the methodology and results proposed by HOBNI that ultimately yield reductions in customer forecasts, particularly for those classes where the customer count is more significant from a revenue perspective. VECC noted that the use of the 2009 exponentially smoothed growth rate pays more mind to the recent declining growth in customer count but ignores the fact that 2009 was a year of economic contraction as compared to 2010 and what is expected in 2011. VECC also indicated that the actual growth rates used were less than the value established through the exponentially smoothing technique. For example, the analysis yielded a growth rate of 2% and 1.3% for residential and GS< 50 classes respectively whereas HOBNI used values of 1.05% and 1.03%. Based on the comparison of HOBNI's forecast for August 2010 to its actual customer numbers for that month, VECC concluded that HOBNI's methodology would under forecast results for the test year.

VECC further submitted that for the Residential and GS<50 classes, the reasonable forecast would be to apply the August 2010 actual customer numbers to the actual growth rate between 2007 and 2009, which would reflect both a year of strong economic growth and a year of economic contraction. Based on the comparison of the forecast and actual August 2010 customer numbers, VECC submitted that the forecast for the GS>50 class would be reduced by 5 customers and the forecast for Intermediate class would be increased by 5 customers. In its submissions, SEC agreed with the adjustments to the GS>50 and Intermediate classes proposed by VECC.

Energy Probe shared VECC's concern about the use of the unproven exponential smoothing methodology. Energy Probe further submitted that a reasonable forecast for Residential and GS<50kW classes would be to apply the 2009 actual customer number to the 2009 actual growth rate for both the bridge and test years. Given that the economy in 2010 and 2011 is expected to be better than in 2009, Energy Probe argued that these forecasts are conservative.

HOBNI responded that exponential smoothing is a commonly used tool for forecasting and that the smoothing of the data itself is not the forecast but the derivation of the data used in the forecast. The Applicant recognized that its annual growth rate of 1.8% is lower than historical years, but submitted that growth rates have been declining. HOBNI's interpretation of the City of Brampton's planning report was that housing connections would remain low in the test years and some slow recovery would start in 2012, but that housing connections would not return to historical high levels until 2015. HOBNI stated that their next cost of service application would capture the increased growth rates applicable to years beyond the current application's test year.

BOARD FINDINGS

While exponential smoothing may be an appropriate tool for forecasting customer additions in some circumstances, the Board is not convinced that the results generated in this instance are appropriate. The Board notes that HOBNI has experienced a relatively strong annual rate of growth of 3.7% in customer additions over the historical period (2005 – 2009) and is not persuaded that the decline in growth rates will continue to even lower levels over the next few years.

The effect of exponential smoothing is that the year 2009, a year of economic downturn, has the most influence on the results. There was little evidence before the Board to suggest that the decline will continue in 2011. The Board recognizes that customer additions may not return to the historically high levels of customer growth seen in earlier years, however to suggest that the rate will continue to decline is also, in the Board's view, unrealistic. Therefore, the Board finds that the growth rate for the 2010 and 2011 bridge and test years should be maintained at the 2009 level of 2.2% annually. In the Board's view, this is a conservative forecast as it is the lowest rate of growth between 2005 and 2009. This 2.2% annual growth rate will result in a total test year forecast of 177,931 customers/connections. The Board finds that the increase of 1,256 (177,931 - 176,675) should be allocated to the residential class. Thus the customer forecast for residential class shall be 124,916.

Other Distribution Revenue

HOBNI forecasted total Other Distribution Revenue of $3,986,412 for the 2011 Test year.

The intervenors raised issues about Miscellaneous Energy Charges and the sale of vehicles being replaced.

SEC also expressed concern that HOBNI had not made a provision for rental income that would be received once tenant space was made available following renovations that were incorporated in to the Company's capital plan.

The intervenors noted that they were unable to reconcile where HOBNI re-allocated $57,025 from Miscellaneous Revenue to account Set up and collection of accounts. VECC submitted that the forecast for Miscellaneous Energy Charges should be increased by $57,000 given the lack of evidence to support the zero forecast for the test year. Energy Probe agreed with VECC.

Energy Probe noted that HOBNI had not included any revenue from the sale of the vehicles which were scheduled to be replaced in 2011. Energy Probe stated that HOBNI claimed that due to the uncertainly of future market values, the forecast of the sales of the vehicles would be close to zero. Energy Probe disagreed and submitted that based on the independent third party Fleet Assessment, half of the estimated gain ($32,500) should be included in the 2011 revenue forecast.

In its reply submission, HOBNI submitted that the gain on sale of vehicles was insignificant and that no further adjustments were required. Regarding Miscellaneous Energy Charges, HOBNI explained that the revenues recorded from 2006 to 2010 were related to one time revenue which will not reoccur in 2011, therefore there is no budget for that in 2011.

BOARD FINDINGS

The historical experience suggests some adjustments to other revenue are warranted and the Applicant has not justified why the two activities identified by intervenors will not continue into the test period. However, the Board finds that the quanta of the two adjustments proposed by intervenors are not material. The Board will not direct the Applicant to make adjustments to its Other Distribution Revenue forecast for 2011 in this instance.

OPERATIONS, MAINTENANCE & ADMINISTRATION ("OM&A")

Intervenors and Board staff both proposed reductions in the applied-for OM&A level on the basis of a line-by-line analysis and from the perspective of the reasonableness of the envelope of total costs. The following areas were addressed in the submissions:

- Overall Increase in OM&A;
- Compensation – 2011 Full Time Equivalent Employees ("FTEEs");
- Compensation – CDM Representative;
- Meter Data Management/Repository ("MDM/R");
- Regulatory Costs;
- Bad Debt Expense;
- Collection Costs;
- Board of Directors Fees;
- Incentive Pay;
- Inflationary Increase;
- Other Miscellaneous costs;
- Incremental OMERS expense;
- LEAP; and
- Harmonized Sales Tax ("HST").

In this section the Board summarizes the submissions of the parties on each of these issues, makes findings on some specific items, and then considers the reasonableness of the envelope of total OM&A costs.

Overall Increase in OM&A

HOBNI is proposing $22,176,435 for its 2011 OM&A expenses. This represents a 24.3% increase over 2009 actual OM&A expenses. The table below presents the OM&A expenses by year.

	2006 Approved	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Bridge Year	2011 Test Year
Operation	$2,720,134	$3,350,836	$3,079,156	$3,544,751	$3,815,041	$4,900,708	$4,559,988
Maintenance	$2,700,089	$3,023,980	$3,091,210	$3,374,105	$3,159,226	$3,590,436	$3,904,606
Billing and Collecting	$3,512,796	$3,775,564	$3,820,263	$4,324,468	$4,897,921	$4,632,782	$5,656,663
Community Relations	$256,376	$1,018,450	$797,999	$371,587	$363,138	$570,000	$640,000
Administrative and General	$4,558,610	$4,986,820	$5,137,182	$5,558,770	$5,601,103	$6,699,374	$7,415,178
Total OM&A	$13,748,005	$16,155,651	$15,925,811	$17,173,680	$17,836,429	$20,393,300	$22,176,435
Year to year % change			*-1.4%*	*7.8%*	*3.9%*	*14.3%*	*8.7%*

SEC submitted that the Applicant's proposal to increase its OM&A costs over a five-year period from $13,748,005 (2006 approved) to $22,176,435 (2011), an increase of 61.3%, is excessive.

SEC provided its OM&A analysis from what it described as both a top-down basis and a bottom-up basis. The top-down approach included a suggested envelope increase based on historic levels of change in overall OM&A. The bottom-up approach was mainly focused on determining an appropriate level of Full Time Equivalent Employees ("FTEEs"). The top-down basis produced a Test Year OM&A budget of $18.7 million and the bottom-up basis, which focuses mainly on personnel costs, produced a Test Year OM&A budget of $19.7 million. SEC recommended the Board allow the higher of the two, which is $19.7 million.

In the top-down approach, a 3% increase compounded annually for five years was used to produce the budget of $18.7 million. SEC suggested this would provide a reasonable level in 2011, since the average increase in OM&A is about 3.35% compounded annually from 2006 to 2009 and the actual OM&A spending in 2010 is an increase of about 2.1% above 2009 as at June 30th, 2010. SEC's recommended OM&A level of $19.7 million was based on the bottom-up approach which will be discussed later in this Decision.

Energy Probe noted that the average increase in the OM&A costs was 3.4% per year for the period from 2006 to 2009, the average increase for the last two years of actual costs (2008 & 2009) was 5.85%. Energy Probe noted that the average increase forecast by HOBNI for 2010 and 2011 was 11.5% which is nearly double the average

rate of increase for 2008 and 2009. Energy Probe submitted that these forecasted annual increases in 2010 and 2011 are not appropriate.

Energy Probe submitted that the maximum increase in OM&A expenses should be 5.5%, which is based on both the average actual OM&A increase in 2008 and 2009 and with the increase recorded in the first half of 2010 on an actual basis. Applying 5.5% to the actual 2009 and 2010 bridge year, the OM&A costs for 2011 test year would be $19,852,391. This represented a reduction of $2,324,044 from HOBNI's 2011 proposed level. Energy Probe also submitted that the reduction of $2,324,044 should then be adjusted for the two new incremental costs for MDM/R and OMERS, which would lead to a net reduction in OM&A costs of $1,190,095 on an envelope basis.

Board staff noted that the proposed 2011 OM&A represented an annual average increase of approximately 12% as compared to the 2006 Board Approved OM&A. In 2009, the OM&A level represented an average increase of 10% as compared to the 2006 level. Board staff submitted that if the Board reduced HOBNI's OM&A for the specific components identified in Board staff's submission, the reduced 2011 OM&A would represent approximately a 10% annual increase from 2006, which would be consistent with HOBNI's historical experience.

VECC did not propose reductions on an envelope basis; however it provided submissions on specific components in OM&A as will be noted below.

In its reply submission, HOBNI stated that the OM&A costs included in the 2006 EDR historical test year were based on the 2004 actual OM&A costs of $13,748,002. The OM&A cost per customer was $129 in 2004 based on the 2004 customer count of 106,526 and the 2004 actual OM&A costs.

HOBNI also argued that if a 3% growth rate is used to calculate the 2011 OM&A costs on a per customer basis, the OM&A costs would be $22,357,125 which is $180,690 greater than the OM&A costs of $22,176,435 submitted in the application. HOBNI further stated that the OM&A costs submitted in the application represented a 2.87% compound growth rate on OM&A costs per customer since 2004 (based on the 2006 EDR historical test year values). Therefore, HOBNI submitted that its OM&A budget of $22,176,435 for the 2011 Test Year is reasonable.

Compensation – 2011 FTEEs

SEC submitted that the Applicant's proposed increases in the workforce have not been justified, and that the budget should reflect a more reasonable level. The Applicant proposed to increase its FTEEs by 39, an increase of 20.3% over five years, of which 20 FTEEs were for 2010 and 2011. SEC concluded that all of the 39 additional FTEEs proposed by HOBNI have been justified primarily because of increasing workload.

SEC noted that a mature utility that has grown by about 10% over the last five years should not need to increase personnel by more than 20%. SEC claimed that normally the increase in FTEEs is about roughly even with customer growth, or at a lesser rate. SEC submitted that the OM&A budget for the Test Year should be set on the assumption that the increase in FTEEs from 2006 actual is no more than the customer growth. As a result, SEC submitted that the increase in FTEEs should be 21, which represented the highest possible customer growth number that could be applied.

Energy Probe noted that a number of the planned hires for 2010 have not been filled but these positions are expected to be filled in 2011. However, Energy Probe submitted that the incremental additions forecast for 2011 had not been adequately justified. The evidence indicated that there are 5 new incremental positions in 2011 and the total costs associated with these positions are $254,516.

Energy Probe submitted that since the increase in 2010 of 14 FTEEs is three times the average increase between 2007 and 2009, there should be no additional FTEEs required for the 2011 test year. The revenue requirement should be reduced by the costs associated with the 5 forecasted positions for 2011 of $254,516.

Energy Probe further noted that the number of FTEEs shown for 2010 and 2011 were seven positions higher than the year-end staff headcount included in HOBNI's IFRS Business Plan, submitted to its Board of Directors for approval on June 9, 2010.

Board staff noted that HOBNI did not identify any replacement positions for the period from 2006 to 2009 and questioned whether the costs had already been included in the existing budget. Board staff submitted that if HOBNI failed to provide a clear explanation, the Board might consider reducing the compensation costs in 2011 by approximately $386,000, which represented the costs associated with four replacement positions.

VECC shared Board staff's concern regarding the change in FTEEs. VECC noted that HOBNI has argued that replacement hires could have filled the positions that have been vacant for some time. VECC further stated that if the replacement positions were all vacant since 2006, it questioned whether it was necessary to rehire for the positions after such a long time. VECC agreed with Board staff's submission that, lacking a clear explanation, the compensation costs for 2011 should be reduced. VECC submitted that the reduction should be the equivalent of at least 3 FTEEs, approximately $290,000.

In its reply submission, HOBNI explained that a number of replacement positions were filled by contract staff in 2009. Subsequently these positions were filled by FTEEs in 2010. This resulted in a higher than normal increase in FTEEs in 2010. HOBNI further explained that if 2009 and 2010 were normalized by including the contract staff in 2009 as FTEEs, this would change the increase in FTEEs in 2009 from four to eight and in 2010 from fourteen to ten. This normalization would result in the increase for 2010 and 2011 being 7.4%, which is in line with historical levels.

HOBNI stated that the costs paid to four contractors were included as administration expenses in OM&A before 2010. HOBNI explained that the replacement positions increased the total compensation amount for 2010, but the costs did not increase the overall OM&A for the period since they were previously included as administration expense. HOBNI submitted that it would not be appropriate to reduce its compensation costs in 2011 by $386,000 for these four replacement positions.

Compensation – CDM Representative

VECC submitted that the Applicant acknowledged that the new CDM position should be excluded from the 2011 revenue requirement; however in its AIC HOBNI did not reflect this adjustment. Energy Probe and Board staff also submitted that HOBNI should reduce its OM&A costs by $70,949. HOBNI agreed to remove $70,949 from its 2011 OM&A proposed budget.

Meter Data Management/Repository ("MDM/R")

Board staff stated that the Board has denied costs related to MDM/R service in its Decision (EB-2010-0219), a smart meter application by PowerStream Inc. and submitted that the Board should disallow any recovery of MDM/R costs at this time. SEC also submitted that the costs should be removed from OM&A. SEC suggests that

the Board will make a generic decision in the future to address this issue which impacts all distributors. This would allow the Board to provide more consistency in addressing these costs.

VECC noted that the IESO has not yet filed an application related to MDM/R costs. The costs provided by HOBNI are therefore based on an estimate. VECC believed that a decision on an IESO MDM/R application will not likely be rendered by the first half of 2011. Therefore, VECC submitted that the proposed MDM/R should be reduced by 50%, or approximately $380,000. VECC also stated that the establishment of a variance account to track the difference in the actual costs is required. Energy Probe took a different position agreeing to include the full amount proposed of $758,949 in the revenue requirement with a variance account to track the difference.

HOBNI responded that if the MDM/R costs are not included in its revenue requirement, its cash flow would be impacted going forward. HOBNI requested the cost estimate be approved and accepted the proposal to establish a variance account.

Regulatory Costs

HOBNI included $1,045,000 in its proposed revenue requirement for costs for activities associated with regulatory matters and the Board's annual assessment costs. Included in the total is an amount of $70,000 for one-time costs associated with the 2011 application. Energy Probe noted that HOBNI has indicated that its next cost of service application would be for rates effective January 1, 2015. Therefore Energy Probe submitted that the regulatory costs of $70,000, which related to this proceeding, should be amortized over the 2011 to 2014 period. The reduction to the revenue requirement would be $52,500. Board staff supported this approach.

HOBNI argued that the regulatory costs of $70,000 are not material, and for that reason, HOBNI proposed no change for this item.

VECC noted that in fact, HOBNI would recover an additional $210,000 over the IRM period if its proposal were accepted. Thus, VECC submitted that the amount of $52,500 should be removed from the 2011 approved OM&A.

Bad Debt Expense

HOBNI's forecasted bad debt expense for 2010 and 2011 is $515,004 and $525,300 respectively. In response to an Energy Probe interrogatory, HOBNI indicated that the most recent year-to-date (June) bad debt expense for 2010 was $143,556. Energy Probe argued that the forecasted 2010 bad debt expense is higher than the annualized 2010 actual expense. Energy Probe submitted that the 2011 expense should be reduced to the average expenses for the period from 2006 through 2008, which is about $334,306, resulting in a reduction of $191,000.

In its reply submission, HOBNI disagreed with the proposed reduction anticipating that further large bankruptcies could and would occur, since the economy has not yet fully recovered. Therefore HOBNI submitted that its forecast is reasonable.

Collection Costs

The forecast collection costs for 2010 and 2011 are $1,027,587 and $1,082,799 respectively. Energy Probe noted that the collection costs for 2009 were $772,456 and the costs of the previous three years averaged just over $600,000 per year. In response to an Energy Probe interrogatory, HOBNI stated that its 2010 year-to-date (June) collection costs were $463,107, which is an increase of 14.2 % as compared to the same period in 2009. Based on this six month period of actual data in 2010, Energy Probe stated that the increase for 2010 should be calculated based on a 14.2 % level of increase over 2009. This would provide a reduction of approximately $145,000 for 2010. For 2011, Energy Probe submitted that the same reduction should be applied and the forecast collection cost should be reduced to $937,800.

HOBNI responded that Energy Probe's proposal is not appropriate stating that based on its experience, collection costs could rise considerably from July through to November. HOBNI proposed no change to its collection costs for 2011.

Board of Directors Fees

Energy Probe indicated that HOBNI included $17,714 in its revenue requirement for the costs related to the Board of Directors of its parent company, Hydro One Inc. Energy Probe submitted that it is inappropriate to include these costs since HOBNI has its own Board of Directors; therefore there is no need to have another oversight from the Board

of Directors of its parent company. Energy Probe also noted that the Board concluded in its Decision (EB-2009-0259) on Burlington Hydro Inc.'s 2009 cost of service application that two layers of Board of Directors fees was not justified.

HOBNI did not reply to this argument.

Incentive Pay

Energy Probe noted that based on its calculation the total cost of the incentive payments included in the revenue requirement is $544,987. Energy Probe had requested that the Applicant provide the allocation of the incentive payments between shareholder value and ratepayer value, but HOBNI was not able to provide this information. Energy Probe submitted that the amount of incentive payments included in the revenue requirement should be reduced from $544,987 to $272,494 to account for only 50% of the incentive payments accruing to the ratepayer.

HOBNI did not respond to this argument.

Inflationary Increase

Energy Probe stated that HOBNI forecasted an increase of $0.6 million related to inflation between 2009 and 2011. These inflation forecasts were based on increases in the Consumer Price Index ("CPI") of 1.9% in 2010 and 2.1% in 2011.

Energy Probe submitted that use of the CPI is not appropriate and argued that the inflationary adjustment should be based on the same inflation factor used by the Board as an IRM adjustment, which is based on the Implicit Price Index for national Gross Domestic Product (GDP-IPI) for Final Domestic Demand. The estimated adjustment for 2011 provided by Energy Probe was 1.25%. Using these factors, Energy Probe submitted that the impact of inflation on OM&A costs should be $375,000, a reduction of $225,000 to the original forecast.

HOBNI did not respond to this argument.

Other Miscellaneous Costs

Energy Probe stated that an update to the OM&A cost drivers table provided by HOBNI indicated that there was a significant increase shown in the “Other” category. The increase for this “Other” category in 2010 is $335,147, but a decrease of $101,106 in 2011. Energy Probe noted that the net increase from 2009 to 2011 is $234,041, which is higher than the average increase over the 2007 to 2009 period of $45,000 per year.

Energy Probe submitted that the increase in the “Other” category should be reduced by $134,000 given that HOBNI did not provide any justification for this increase in 2010. In fact, Energy Probe noted that this proposed reduction is similar to the corrections noted in response to Energy Probe interrogatory #35, related to double counting for postage and stationary costs and information system expenses. In response to that interrogatory, HOBNI noted that these costs should in fact be excluded to avoid double counting.

HOBNI did not respond to this argument.

Incremental OMERS expenses

HOBNI stated that the increase in contributions to the OMERS pension plan would be about $1.5 million for the period from 2011 to 2014. Board staff submitted that the amortized incremental amount should be included in HOBNI’s revenue requirement and it should be $375,000.

SEC and Energy Probe both supported including $375,000 in 2011 OM&A costs. In addition, Energy Probe submitted that it is appropriate to establish a variance account to track the difference.

In its reply submission, HOBNI agreed with Board staff’s submission on the inclusion of the incremental OMERS expense in the revenue requirement and withdrew its request for a variance account.

Low Income Energy Assistance Program (“LEAP”)

HOBNI updated its OM&A costs to reflect costs related to LEAP. Board staff noted that $75,000 was included in HOBNI’s OM&A. However, it submitted that the final amount

should be adjusted in the draft Rate Order to account for any changes in the service revenue requirement as a result of this Decision.

Harmonized Sales Tax ("HST")

Board staff stated that the provincial sales tax ("PST") and goods and services tax ("GST") were harmonized effective July 1, 2010. Due to the harmonization of the PST and GST, utilities might benefit from a reduction in OM&A expense and capital expenditures. Board staff noted that HOBNI made further adjustments to its revenue requirement to reflect all cost reductions in OM&A ($105,000) and capital expenditures ($411,000). Board staff had no concerns with respect to the reductions that HOBNI has made to reflect its forecasted PST savings.

BOARD FINDINGS

The Board finds that it is appropriate to adjust the requested OM&A for the following items:

- MDM/R costs should be excluded because of the uncertainty of the timing and the cost recovery mechanism flowing from any application by the IESO to recover these costs.
- HOBNI has agreed that its CDM representative costs should be removed, but this was not reflected in the OM&A costs provided by HOBNI in its AIC.
- The request for the Board of Directors fees results from there being two layers of oversight for HOBNI, which is not justified in the circumstances.
- One-time regulatory costs should be amortized over a four-year period.
- The Board agrees with Energy Probe that an adjustment to the factor used for inflation is warranted. The Board has limited inflationary increases for non-labour expense forecasts to the GDP-IPI level in other cost of service applications[2] and will do so in this case as well. On February 28, 2011, Statistics Canada published the change for 2010 over 2009 as part of the National Economic Accounts. The percentage change is 1.3%.

[2] For example, Decision on Innisfil Hydro Distribution Systems Limited (EB-2008-0233), p.12, Decision on COLLUS Power Corp. (EB-2008-0226), p. 12.

- The Board agrees with Energy Probe that the ratepayers should incur only the incentive payments accruing to the ratepayer. Since HOBNI did not provide evidence to support an allocation of the incentive payment between shareholder and ratepayer, nor the factors that went in to the determination of incentive pay, the Board will allocate 50%, or $272,494, of the incentive payment to the shareholder. This amount will therefore be excluded from the revenue requirement.

After making these adjustments, the Board notes that the remaining OM&A is approximately 16% higher than 2009 actual spending, an average of approximately 8% per annum. Given the relatively modest growth in customers forecast for the test period, and the relatively modest rate of inflation, and the lack of any compelling evidence why a large increase is warranted, the Board finds this increase to be excessive. The Board finds that an increase of 10% over 2009 actual spending is reasonable. Given the 2.2% per annum forecast growth in customers, this allows for slightly less than 3% per annum increase in spending per customer, which is more than the rate of inflation. This will result in an overall OM&A budget of $19,620,000 excluding the increase to OMERS and LEAP.

The Board accepts the reductions already made by the Applicant as of the close of the record associated with HST, the incremental OMERS expenses of $375,000 and the increase to the revenue requirement at the time of the draft Rate Order for LEAP.

The Board is not inclined to delve into the specific numbers of FTEEs or the impact of whether work is done by full time staff or contracted out. That is a matter for HOBNI to manage within this spending envelope.

PAYMENTS IN LIEU OF TAXES ("PILs")

Energy Probe noted that HOBNI's PILs calculation did not include the small business deduction credit since it was not aware of its eligibility and indicated that HOBNI confirmed, in response to undertaking J1.4, its eligibility of this credit. Energy Probe submitted that based on its calculation the small business deduction credit would reduce income taxes by $36,250.

Energy Probe further argued that HOBNI did not take into account other deductions in its PILs calculation, such as Apprenticeship Training (federal or provincial) and Cooperative Education tax credits. Energy Probe submitted that the aggregated tax credits of $100,000 should be included in HOBNI's 2011 PILs calculation.

SEC agreed with and adopted Energy Probe's submission.

Board staff noted that in the event the Board makes changes to HOBNI's rate base, capital and operating expenditures, HOBNI should update its PILs calculation to reflect any impact arising from the changes.

In its reply submission, HOBNI did not respond to these arguments.

BOARD FINDINGS

The Board accepts Energy Probe's approach to PILs to include the small business deduction credit and other deductions, such as Apprenticeship Training (federal or provincial) and Cooperative Education tax credits in the determination of HOBNI's PILs calculation. The Board notes that the level of PILs will be updated on the basis of the Board's findings regarding the rate base, capital and operating expenditures. The draft Rate Order should provide sufficient details of the calculations.

DEPRECIATION

HOBNI updated its depreciation rates as a result of a study by Foster Associates Inc. Board staff, Energy Probe, SEC and VECC had no concerns with the new depreciation rates proposed by HOBNI.

BOARD FINDINGS

The Board finds that the proposed depreciation rates based on a study prepared by Foster Associates Inc. are reasonable and that the overall depreciation expense is appropriate and consistent with the Asset Amortization Study prepared by Kinectrics Inc. The Board notes that the final depreciation expense will be determined on the basis of the Board's findings regarding capital expenditures and directs HOBNI to update the depreciation expenses in its draft Rate Order.

RATE BASE AND CAPITAL EXPENDITURES

HOBNI requested approval of an updated rate base of $331.0 million in this application, composed of $277.4 million in average net fixed assets and $53.6 million in working capital allowance.

The following areas are addressed in this section:

- Capital Expenditures
- Working Capital Allowance
- Green Energy Act Plan

Capital Expenditures

HOBNI proposed capital expenditures of $22,681,013 in 2011. The costs related to the Green Energy Act Plan expenditures have been excluded from the rate base.

VECC objected to the inclusion of capital expenditures of $304,643 for 2010 related to the renovation of space vacated by a previous tenant and an additional $60,000 for the reconfiguration of the associated parking area. VECC stated that HOBNI had indicated that it would proceed with this expenditure only if a new tenant was located. However, at the oral hearing, HOBNI confirmed that no tenant had yet been found and it would not use the space for its own purposes. VECC submitted that the total of $364,643 should therefore be excluded from the 2011 rate base and that the amount would need to be adjusted on a CGAAP basis since it reflects IFRS accounting standards as originally proposed by HOBNI in its application.

Energy Probe also argued that as HOBNI has no need for these premises in 2010 or 2011, the total of $364,643 should be removed from the calculation of the test year rate base, and the associated depreciation expense should be excluded from the 2011 revenue requirement.

SEC argued that if capital expenditures on space vacated by a previous tenant were approved by the Board, then a provision for rental income should be included in the Other Distribution Revenue. In response to Energy Probe IR #29, HOBNI identified an amount of $34,000 in revenue reduction that was related to daycare rental fees that were no longer being collected.

HOBNI did not respond to the parties' arguments on this item.

Energy Probe noted that the amount of $137,198 of 2010 capital expenditures related to the chassis for a bucket truck that would go into service in 2011. Since this expenditure is only used and useful when the entire vehicle is in service in 2011, Energy Probe submitted that $137,198 should be removed from 2010 rate base and added to the 2011 rate base.

In its reply submission, HOBNI clarified that the amount of $137,198 related to chassis costs had not been included in 2010 rate base. The costs were included as part of Construction In Progress balances.

Energy Probe also noted that the net book value of the replacement vehicles in 2011 has not been excluded from 2011 rate base. Energy Probe submitted that the value of 2011 rate base should be reduced by $73,250 to reflect vehicles that are no longer use and useful. Energy Probe further submitted that the depreciation expense associated with the replacement vehicles in 2011 should also be reduced.

VECC agreed with both issues identified by Energy Probe in regards to the vehicle expenditures.

BOARD FINDINGS

The Board agrees with the intervenors that the capital expenditures related to the renovation of space vacated by a previous tenant and the reconfiguration of the associated parking area (a total of $364,643) should be excluded from rate base. Given that HOBNI has not included the associated rental income in Other Distribution Revenue, the Board would expect that the space will not be required and the capital expenditures for renovation should not be needed. Therefore the capital expenditures of $364,643 should be removed from rate base.

The Board finds that the issue of replacement vehicles is not material and will not make any adjustment.

Working Capital Allowance

VECC noted that HOBNI has used the RPP price to value all of its purchases to calculate its cost of power when 65% of its volumes are non-RPP. VECC further noted that the Board has approved working capital commodity cost of power calculations based on different pricing for RPP versus non-RPP volumes. Using a two pricing approach, the commodity cost of power would be reduced from $270,480,528 to $257,805,304.

VECC further argued that with the recent October 2010 RPP Report issued by the Board, the prices related to RPP and non-RPP volumes are available. Based on the latest information, VECC submitted that the commodity cost of power for 2011 should be $259.6 million and this should be used to establish HOBNI's working capital allowance, subject to change based on the final approved 2011 load forecast.

Energy Probe and SEC agreed.

In its reply submission, HOBNI agreed to adjust is commodity cost of power to reflect different pricing for the RPP/non-RPP volumes.

BOARD FINDINGS

The Board accepts that the commodity cost of power should be determined in a way that reflects the different pricing schemes for the RPP and non-RPP volumes. The Board directs HOBNI to update the cost of power used in calculating its working capital allowance to reflect the most recent October 2010 RPP Report.

The cost of power should also be updated to reflect the load forecast as approved in this Decision and the updated retail transmission rates reflecting the latest approved uniform transmission rates.

Green Energy Act Plan

HOBNI submitted its Green Energy Act Plan ("GEA Plan") as part of its original application on June 30, 2010. HOBNI has requested GEA Plan expenditures in rate base of $1,003,000 for 2010, and $1,024,000 for 2011. These expenditures relate to Expansion, Renewable Enabling Improvement (REI) and Smart Grid.

During the proceeding, HOBNI filed a letter with the Board withdrawing its request for GEA Plan expenditures for inclusion in rate base. Instead, HOBNI requested that expenditures be tracked through variance/deferral accounts and that an equivalent funding adder based on $163,967 per annum to cover the revenue requirement impact of the current proposed spending be approved. The proposed funding adder is a fixed charge of $0.10 per month, per metered customer.

In response to intervenors' examination and submissions, HOBNI stated in its AIC that it would revise its GEA Plan funding adder request to only include HOBNI's share of GEA related costs. HOBNI submitted in its AIC that, "[HOBNI] would accept revising the funding adder to include Brampton's customers' share of GEA-related costs, in addition to maintaining a variance account for said costs." Such a revision has the effect of reducing the funding adder below $0.10 per month per metered customer.

HOBNI's application in respect of the GEA Plan appears to be modeled on the approach used to fund smart meters:

1. A funding adder to recover the revenue requirement impact of HOBNI's customers' share of GEA-related costs.
2. Approval of a deferral account to record the spending and revenue of GEA-related spending.
3. No finding of prudence of the expenditures until HOBNI applies for disposal of the deferral account.
4. Approval of HOBNI's proposed direct benefits attribution.

Deferral Account Treatment

All parties agreed that it was premature for the Board to find that GEA Plan expenditures are prudent at this time and agreed that a funding adder calculated to recover the revenue requirement impact of HOBNI's customers' share of GEA Plan related costs should be approved by the Board.

Direct Benefit Attribution

The Board issued a Decision with Reasons on July 22, 2010 that established the Renewable Generation Connection Rate Protection Compensation Amount ("RGCRP")

for HONI for 2010 based on HONI's provisionally approved amounts and direct benefit percentages.

Board staff submitted that the RGCRP Decision clearly set out how the amounts are to be collected by the IESO and paid to eligible distributors. Board staff further submitted that a similar decision for HOBNI's RGCRP amount could be rendered shortly after HOBNI's rates decision is issued in the current proceeding.

Board staff noted that the parties and the Applicant had agreed that the following would be tracked in a variance account, should the Board so decide:

1. Any variance related to final approved percentages for direct benefits and those approved by the Board in this application; and
2. Any variance between expenditures budgeted and actually incurred with respect to GEA Plan spending in 2010 and 2011.

Under section 79.1 of the Act some of the Board-approved costs incurred by a distributor to make an eligible investment for the purpose of connecting or enabling the connection of a renewable energy generation facility to its distribution system may be recovered from all provincial ratepayers rather than solely from the ratepayers of the distributor making the investment.

Direct benefits are those that are attributable to only the customers of the distributor making the investment and where the benefits are readily quantified in monetary terms. These benefits are often represented in percentage terms according to the type of investment. While HOBNI and the parties agreed on the allocation in regards to Expansions and Smart Grid, there was disagreement in regards to REI in general and as it pertains to investments in SCADA.

Direct Benefit Allocation

	Proposed by HOBNI		**Proposed by Board staff**	
	Provincial Ratepayers	**HOBNI Customers**	**Provincial Ratepayers**	**HOBNI Customers**
Expansions (up to threshold)	81.25	18.75	81.25	18.75
Renewable Enabling Improvements	100	0	94	6
SCADA	50	50	94	6
Smart Grid (Other)	0	100	0	100

Board staff submitted that it was not convinced that REI would provide no benefit to load customers from an operational and reliability standpoint and submitted that absent a distinguishing feature of HOBNI's system that renders the default percentage set in HONI's case inapplicable, it would be inappropriate to apply a different percentage at this time. Board staff submitted that the default HONI percentages for REI would be most appropriate at this time. VECC submitted that HOBNI had adequately explained why REI spending is of no direct benefit to its own ratepayers.

SEC agreed with Board staff's submissions with respect to the appropriateness of direct benefits.

HOBNI disagreed with Board staff's comment that Board staff were not convinced that REI would not benefit load customers from operational and reliability standpoints. HOBNI indicated that these expenditures are only for monitoring purposes—i.e. to send data and status information back to the transmitter. HOBNI argued that the stated functionality supported its view that 100% of the expenditures should be allocated to provincial ratepayers.

Board staff submitted that the appropriate percentage for SCADA investment is 6% for HOBNI ratepayers and 94% for provincial ratepayers citing a number of references to these investments supporting enabling generation, and a lack of detailed analysis. VECC submitted that, "HOBNI has confirmed that its current SCADA system is adequate for purposes of serving its ratepayers and that the investment would not proceed, save for the connection of new distribution generation."[3] VECC also submitted that, in general, direct benefit attribution should be based on the provisionally approved percentages in HONI's case.

HOBNI proposed and parties agreed that investment in SCADA should be considered REI; however parties disagreed that only 6% of SCADA expenditures would benefit HOBNI ratepayers. While the initiation of the SCADA project was driven by renewable generation, HOBNI submitted that the SCADA expenditures will benefit both the load and generator customers 'equally' by providing operational and reliability benefits to the load customers. Therefore, HOBNI submitted that the allocation should be maintained at a 50-50 split.

[3] Tr. Vol. 1 December 6, 2010, pg. 102-103

Quanta of Green Energy Plan Expenditures for Approval and Recovery

Board staff submitted that HOBNI's application for funding adders to recover costs in lieu of inclusion of expenditures in rate base is reasonable. However, Board staff did not agree with the quanta of costs for recovery.

Board staff submitted that the funding adder should be recalculated on the basis of the direct benefit percentages provided by Board staff. Board staff indicated that all revenues collected and costs incurred with respect to GEA Plan expenditures should be tracked with funding adders in the deferral accounts.

VECC submitted that the GEA funding adder should be calculated using the percentages provisionally approved for HONI. SEC made a similar submission, that it would be inappropriate for HOBNI to recover 100% of costs from ratepayers, and then refund whatever is over collected once the final direct benefits percentages are determined.

VECC also submitted that the recovery of the GEA funding adder should be done on a volumetric basis as opposed to on a fixed adder per metered customer basis. HOBNI made no reply submission on VECC's submission for a volumetric adder.

In its reply submission, HOBNI agreed that all the costs incurred and revenues collected with respect to GEA Plan expenditures should be tracked in the deferral accounts. As previously noted, HOBNI indicated in its AIC that it would revise the funding adder to include only Brampton's share of GEA-related costs. HOBNI agreed that it would track the funding adders for renewable generation and smart grid in Account 1533 and 1536, respectively.

BOARD FINDINGS

In its report entitled *Framework for Determining the Direct Benefits Accruing to Customers of a Distributor under Ontario Regulation 330/09* (EB-2009-0349), the Board established its policy regarding the allocation of Board-approved costs incurred by a distributor to make an *eligible investment* for the purpose of connecting or enabling the connection of a renewable energy generation facility to its distribution system that may be recovered from all provincial ratepayers rather than solely from the ratepayers of the distributor making the investment.

For distributors that file a Basic GEA Plan, such as HOBNI, the report indicates that a basic (i.e., standardized) direct benefit assessment will be applied. The standardized direct benefit assessment was approved in the Rate Order for Hydro One Distribution (EB-2009-0096). These provisional direct benefit percentages are 17% for expansion investments and 6% for REI investments. The Board is not persuaded that it should deviate from the standardized assessment and apply the percentages proposed by HOBNI's for its GEA Plan expenditures. The direct benefit percentages applied in HONI's case, EB-2009-0096, shall apply to HOBNI on a provisional basis. In applying the provisional direct benefit percentages to HOBNI, SCADA shall be considered REI investment, and attract the default percentage.

In this report the Board articulated its view that it considers this approach to be transitional and evolutionary. The Board therefore finds that a funding adder and deferral account is the most appropriate mechanism in this case. The Board will approve a funding adder based on the direct benefit assessment set out in EB-2009-0096. The Board approves the proposed expenditures for the purposes of recording HOBNI's customers' share of costs in a deferral account. A prudence review will occur at the time HOBNI seeks disposal of the deferral account.

With respect to "Smart Grid (Other)" investments, the Board accepts HOBNI's position, and the submissions of Board staff, that these investments are ineligible for direct benefit attribution and provincial recovery. The Board's Report clearly defines Smart Grid investments as ineligible unless the investment has been identified in the Distribution System Code as a Renewable Enabling Improvement.[4] Therefore, 100% of "Smart Grid (Other)" investment shall be recovered from HOBNI's ratepayers.

The Board directs HOBNI to recalculate the GEA funding adder to reflect only amounts that will be collected on a provisional basis from its own ratepayers. The balance of the GEA funding adder will be collected through a RGCRP amount set by the Board, and then collected by the IESO and paid to eligible distributors, such as HOBNI. In its draft Rate Order, HOBNI shall identify the derivation and quantum of the revised GEA funding adder per this Decision, as well as the resulting provincial ratepayer's share.

The amounts collected by the IESO and paid out through this process will be tracked using Account 1533. It will be necessary to use sub-accounts to separate collection from HOBNI's ratepayers and provincial ratepayers (i.e. payments from the IESO) so

[4] Ibid pg. 3, bullet 2

that the necessary reconciliation can be made when direct benefit percentages are finalized. The Board's Guidelines (G-2009-0087) created two deferral accounts for the recording of renewable connection expenditures: account 1531 for capital costs and account 1532 for OM&A costs. HOBNI should use these accounts to record actual expenditures related to renewable energy generation connections.

The Board is satisfied with the nature of the costs, but does not have sufficient information to determine the final quantum of costs. The Board will leave a determination on prudence of the GEA Plan expenditures to a later date when better information is available.

The GEA funding adder will be collected from all HOBNI metered customers as a fixed charge. Given the quantum of the funding adder and the limitation of a four decimal volumetric adder available on customer bills, a fixed charge is the only practical way to collect these amounts from customers at this time. The Board notes that this is not its preferred approach. The fixed charge should be reviewed and replaced with a volumetric charge as the transitional framework evolves, the percentages are finalized, and the amounts involved are large enough to do so effectively.

COST OF CAPITAL

HOBNI's proposed test year Cost of Capital as set out in the original application is summarized in the following table.

Cost of Capital Parameter	HOBNI's Proposal
Capital Structure	60.0% debt (composed of 56.0% long-term debt and 4.0% short-term debt) and 40.0% equity
Short-Term Debt	2.07%,
Long-Term Debt	6.76%
Return on Equity (ROE)	9.92%
Weighted Average Cost of Capital	7.84% as proposed, but subject to change as the short-term and ROE are updated per the Board Report at the time of the Board's Decision.

In 2009, the Board conducted a consultation to review the cost of capital for all rate regulated utilities. On December 11, 2009, the Board issued its *Report of the Board on the Cost of Capital for Ontario's Regulated Utilities* (the "2009 Report").

On November 15, 2010, the Board issued a letter documenting the updated Cost of Capital parameters to be used in the 2011 cost of service applications for rates effective January 1, 2011. These are summarized in the following table:

Cost of Capital Parameter	**Updated Value for 2011 Cost of Service Applications for rates effective January 1, 2011**
Return on Equity	9.66%
Deemed Long-term Debt Rate	5.48%
Deemed Short-term Debt Rate	2.43%

Long-Term Debt Rate

In Exhibit 5 of its application, HOBNI stated that its Long-Term Debt rate was determined based on the weighted average debt rate of its existing and new debts. The Applicant used debt rates for the new debt issued in 2010 and 2011 based on the October 2009 Consensus Forecasts. However, during the course of the proceeding, HOBNI updated its forecasts related to the need for long term debt. HOBNI did not update its forecast debt rates.

Long-Term Debt

Description	Issue Date	Debenture ($M)	Updated[5] ($M)	Debt Rate
Debt through parent company public debenture issue	2001	143	143	6.95%
New Debt to be issued through parent in 2010	2010	10	0	5.71%
New Debt to be issued through parent in 2011	2011	47	42	6.41%
		200	185	6.76%*

*This debt rate is based on HOBNI's original proposal and has not been revised to reflect the updated amounts.

Energy Probe submitted that the forecasted debt rate used by HOBNI is out of date and should be updated using the Cost of Capital parameters set in the Board's letter dated November 15, 2010, which documented a Deemed Long-term debt rate of 5.48%. Energy Probe further calculated that based on the updated Deemed Long-term debt rate of 5.48% and $42 million of new debt for 2011, the weighted average long-term debt rate would be changed from 6.76% to 6.62%. Board staff filed a similar submission.

[5] Tr. Vol. 1 pp. 151 - 153

VECC also noted that the proposed new debt for 2011 should reflect the more up-to-date forecast. HOBNI provided its assumed (forecasted) rate for 30-year debt of 5.94% and for 10-year debt of 5.09%. Based on this information, VECC submitted that the assumed debt rate for 2011 should be based on the average of 5.09% and 5.94%, which is 5.52%.

SEC took a different position and submitted that the appropriate debt rate is the weighted average cost of long term debt of HONI which was determined to be 5.67% in the recent Hydro One Transmission Case (EB-2010-0002). This approach, in SEC's view, would avoid a regulated entity from earning a speculative profit by re-lending to a regulated subsidiary at a higher rate.

HOBNI clarified that it is a subsidiary of HOI and a sister utility of HONI and that the cost of debt associated with HONI is not related to HOBNI. The existing debt that HOBNI had is with HOI, not HONI.

HOBNI responded that it would be inappropriate to update the debt rates forecast for 2011 as suggested by intervenors. HOBNI stated that its forecast was completed based on the best information available at the time. HOBNI submitted that it is neither practical nor appropriate to update all assumptions included in the application prepared several months ago.

BOARD FINDINGS

The Board expects HOBNI to update its cost of capital for ROE and Short-term Debt rate based on the parameters issued by the Board in its letter on November 15, 2010.

While the Board is normally reluctant to make selective updates to an application, it has been the Board's practice to update cost of capital parameters, including rates associated with debt instruments that the Board has decided should attract the Board's deemed rate. As affiliate debt, HOBNI's proposed 2011 long term debt is in that category. Based on the record, particularly Exhibit 5/Tab1/Schedule 2.0/Table 3 and the associated documentation on pages 3 and 4 of that exhibit, it is clear that the rate of 6.41% for the new debt expected for 2011 is a methodological forecast using an approach analogous to that used by the Board to calculate the deemed long-term debt rate in accordance with the 2009 report. Given that the rate for the 2011 new debt is a formulaic forecast, the Board finds that the rate should reflect the most recent data. In

this case, the Board finds that the deemed long-term debt rate of 5.48%, as documented in its November 15, 2010 letter, should apply to the new long-term debt of $42 million expected in 2011.

Approved weighted average long-term debt rate

Description	Issue Date	Updated ($M)	Debt Rate
Debt through parent company public debenture issue	2001	143	6.95%
New Debt to be issued through parent in 2011	2011	42	5.48%
		185	6.62%

HOBNI should update its long-term debt forecasts to reflect the most recent data. The Board finds that the debt rate associated with the new $42 million note to be issued in 2011 should be 5.48% and the weighted average debt rate should be 6.62%.

COST ALLOCATION AND RATE DESIGN

The following issues are addressed in this section:

- Revenue-to-Cost Ratios
- Monthly Service Charges (“MSC”)
- Transformer Ownership Allowance
- Retail Transmission Service Rates (“RTSR”)
- Low Voltage Charges
- Loss Factors

Revenue-to-Cost Ratios

The following table sets out HOBNI’s approved 2006, current and proposed revenue-to-cost ratios and the Board’s targets, as established in the Board’s *Application of Cost Allocation for Electricity Distribution’s EB-2007-0667*.

Revenue-to-Cost Ratios

Customer Class	Column 1 2006 Approved Ratios	Column 2 Current Ratios	Column 3 Proposed Ratios for Test Year	Column 4 Board Target Range
Residential	105.80%	102.45%	101.12%	85% - 115%
GS < 50 kW	122.38%	129.80%	120.00%	80% - 120%
GS 50 to 699 kW	64.05%	71.68%	80.00%	80% - 180%
GS 700 to 4,999 kW (Intermediate)	149.68%	150.17%	130.00%	80% - 180%
Large User	95.39%	100.01%	100.00%	85% - 115%
Unmetered Scattered Load	87.52%	77.71%	80.00%	80% - 120%
Street Lighting	10.63%	12.40%	70.00%	70% - 120%

Board staff submitted that the proposed ratios are all within the Board's target ranges. However, Board staff noted that the revenue-to-cost ratio for the Street Lighting class in the application would increase from 12.40% to 70% in one step. In order to mitigate approximately 31% total bill impacts, Board staff proposed a two year phase-in approach for the Street Lighting class to be achieved in equal increments, and that the shortfall in revenue arising from its proposal be recovered from the GS 700 to 4,999 kW class.

Energy Probe submitted that the proposed revenue-to-cost ratios are appropriate. Energy Probe also noted that if the Board determined that the movement for the Street Lighting class from 12.40% to 70% is excessive, that this ratio should be increased to 41.2% in 2011, with further increase to 70% in 2012.

SEC and VECC both submitted that HOBNI's proposed revenue-to-cost ratios are appropriate.

HOBNI did not reply to the submissions on its revenue-to-cost ratios.

BOARD FINDINGS

The Board is concerned that the proposed revenue-to-cost ratios for the Street Lighting class will result in a significant bill impacts. The Board agrees with the proposal to move the revenue-to-cost ratio for Street Lighting class to 41.2% in 2011 with a further increase to 70% in 2012 and that the shortfall in revenue arising from its proposal should be recovered from the GS 700 to 4,999 kW class. The Board accepts the proposals for the rest of the classes as filed and shown in Column 3 in the above table.

Monthly Service Charges ("MSC")

HOBNI is proposing to maintain the same fixed/variable proportions for all the classes, except the Street Lighting class. For the Street Lighting class, the MSC was set based on the aggregate fixed/variable split for total distribution revenue, since it currently has no MSC.

Board staff and Energy Probe supported that the current fixed/variable proportions should be maintained.

SEC noted that the current MSC for GS>50 kW already exceeds the upper bound of the band and the proposed MSC would move further away from the upper band. SEC submitted that the MSC for GS>50 kW should remain at the 2010 level, and the revenue shortfall should be made up in the volumetric charge for the class.

VECC submitted that the MSC for GS>50 kW and Large Use classes should be maintained at the 2010 level. VECC explained that where the current MSC is above the upper band, the Applicant should not increase them further, even if its proposal was to maintain the existing fixed/variable proportions.

Parties had no concerns with respect to the MSC for the Street Lighting class.

In its reply submission, HOBNI acknowledged that in some cases the upper band of the MSC was exceeded, but it submitted that to maintain the existing fixed/variable split is consistent with the Board's Cost Allocation Report and previous decisions.

BOARD FINDINGS

The Board accepts HOBNI's proposed MSC which maintains the current fixed/variable proportions. The Board notes that this is consistent with other decisions[6] in which it has approved applications to increase MSC that were already above the cost allocation ceiling, provided that the increase would not result in a higher revenue from the fixed charge relative to the volumetric charge.

[6] Decision on Lakeland Power Distribution Ltd. (EB-2008-0234), p.29-30, Decision on London Hydro Inc. (EB-208-0235), p.42-43.

Transformer Ownership Allowance

HOBNI is proposing to change its Transformer Ownership Allowance to $0.7048 per kW for the GS >50 to 699 kW class and $0.8758 per kW for the GS 700 to 4,999 kW class.

Board staff submitted that HOBNI's proposals are reasonable.

Energy Probe, SEC, VECC made no submissions on the change to the Transformer Ownership Allowance.

BOARD FINDINGS

The Board accepts the Transformer Ownership Allowances for the GS >50 to 699 kW class and the GS 700 to 4,999 kW class as proposed by HOBNI.

Retail Transmission Service Rates ("RTSR")

In response to a Board staff interrogatory, HOBNI requested a reduction in its RTSR for all classes. HOBNI's updated RTSRs are based on the model provided by Board staff on August 20, 2010. This model assists electricity distributors to adjust their RTSRs based on a comparison of historical transmission costs adjusted for Ontario Uniform Transmission Rates ("UTRs") levels and revenues generated under existing RTSRs.

Board staff and VECC submitted that HOBNI should update its RTSRs for the most recent Board approved UTRs as part of its draft Rate Order.

HOBNI responded that it would use the most recent RTSRs to update its rates by customer classes once the Decision of this application has been issued.

BOARD FINDINGS

The Board notes that a rate order was issued on January 18, 2011 approving new uniform provincial transmission rates (EB-2010-0002). The changes in the UTRs effective January 1, 2011 are shown in the following table.

Uniform Transmission Rates

	Effective on January 1, 2011
	($/kW/month)
Network Service Rate	3.22
Line Connection Service Rate	0.79
Transformation Connection Service Rate	1.77

The Board directs HOBNI to update its RTSRs accordingly in its draft Rate Order.

Low Voltage Charges

HOBNI is proposing to remove its proposed LV costs for 2011 from its 2011 revenue requirement because of the low cost levels. The LV costs instead would be recorded in account 1550 directly on an annual basis; the disposition of account 1550 would then be processed annually during the IRM process, as outlined in the *Report of the Board on Electricity Distributor's Deferral and Variance Account Review* ("EDDVAR").

Board staff and VECC submitted that given the materiality, the removal of HOBNI's LV costs from the revenue requirement is appropriate.

BOARD FINDINGS

The Board accepts HOBNI's proposal of excluding its LV costs from the revenue requirement. The Board notes that the LV costs will continue to be recorded in account 1550 and agrees that the disposition process for account 1550 will follow the guidelines stated in EDDVAR.

Loss Factors

HOBNI applied for a Total Loss Factor ("TLF") of 1.0349 (for secondary metered customers < 5,000 kW) based on an underlying Distribution Loss Factor ("DLF") of 1.0324 and Supply Facility Loss Factor ("SFLF") of 1.0025. The proposed SFLF and DLF are based on the average of five historical years 2005 to 2009. The current approved TLF for secondary metered customers < 5,000 kW is 1.0356.

VECC noted that HOBNI's proposed loss factors are based on a five-year historical average and the past loss factors have been fairly consistent. VECC submitted that the proposed loss factors should be accepted.

Board staff had no concerns with respect to the proposed loss factors. No other intervenor commented on the proposed loss factors.

BOARD FINDINGS

The Board accepts the TLFs proposed by HOBNI. The TLFs are set out in the table below.

Total Loss Factors

Secondary metered < 5000 kW	1.0349
Primary metered < 5000 kW	1.0247
Secondary metered > 5000 kW	1.0145
Primary metered > 5000 kW	1.0045

DEFERRAL AND VARIANCE ACCOUNTS

The following issues are addressed in this section:

- Balances Proposed for Disposition
- New or Continued Deferral and Variance Accounts
- PILs Account 1562

Balances Proposed for Disposition

HOBNI stated that it received the Board's approval on April 13, 2010 to dispose its Group 1 deferral and variance account balances as of December 31, 2009. HOBNI is requesting disposition of the following Group 2 deferral and variance account principal amounts as at December 31, 2009 and the forecasted interest through December 31, 2010 over a two year period.

Account Balances for Disposition

Description	Account	Principal Amounts as of Dec. 31/09 $	Balance for Disposition including forecast interest to Dec. 31/10 $
Other Regulatory Assets	1508	204,933	76,738
RCVA – Retail Cost Variance Account - Retail	1518	65,359	112,023
RCVA – Retail Cost Variance Account – STR	1548	1,098	10,105
Deferred Payments in Lieu of Taxes	1562	4,139,347	5,592,315
RSVA – One-time Wholesale Market Service	1582	1,045,186	1,362,967
2006 and Subsequent Years' PILs and Tax Variance	1592	(558,645)	(605,752)
Total		**4,901,278**	**6,548,396**

HOBNI stated that for the period beginning May 1, 2006, account 1592 was used to record the tax impact of changes in tax legislation and the balance above reflected the reduction in Ontario Capital tax rates and increased limits in 2007 and 2008.

Board staff submitted that it had no concerns with the balances proposed for recovery and the period for disposition other than for account 1562.

VECC also submitted that it had no submission regarding the balances proposed for recovery for accounts 1508, 1518, 1548, and 1582. With respect to the disposition period, VECC submitted that if the Board decided to defer its decision or to reduce the disposition amount for the PILs related accounts substantially, then a one year disposition period would be appropriate. Energy Probe shared the same view.

BOARD FINDINGS

The Board approves the account balances for account 1508, 1518, 1548, 1582 and 1592 as presented by HOBNI and approves a disposition period of one year. The Board will make findings for account 1562 in the PILs section below.

New or Continued Deferral and Variance Accounts

In its Application, HOBNI requested the establishment of a variance account for Recovery of Late Payment Settlement costs and three IFRS related deferral accounts.

These requests were withdrawn by HOBNI in its reply submissions.

In regards to the request to establish a deferral account for MDM/R costs, Board staff submitted that the Board had denied such a request in its decision on PowerStream Inc.'s smart meter application (EB-2010-0209). SEC agreed with Board staff that the Board should maintain consistency with its decision unless the current situation is materially different.

Energy Probe and VECC however supported the establishment of a new variance account for MDM/R costs.

HOBNI responded that it is appropriate to recover the MDM/R costs in order to mitigate future rate shock to its customers.

BOARD FINDINGS

The Board denies HOBNI's request to establish a deferral account for MDM/R costs. The Board notes that while O. Reg. 453/06 permits the IESO to recover its costs of the MDM/R, it must be through a Board order. Therefore, an application would first have to be filed with the Board. The Board has no indication at this time of the magnitude or timing of such an application. Furthermore, O. Reg. 453/06 does not indicate from whom the costs will be recovered.

Once these issues have been dealt with by the Board, there may well be a deferral account established to allow distributors to track these costs.

PILs Account 1562

HOBNI is requesting disposition of the balances in deferred payments-in-lieu of taxes ("PILs") account 1562. HOBNI has proposed a debit balance for disposition in account 1562 of $5,592,315. Debit balances are recoveries from customers.

In 2001, the Board approved a regulatory PILs tax proxy approach for rate applications coupled with a true-up mechanism[7] filed under the Reporting and Record-keeping Requirements to account for changes in tax legislation and rules and to true-up between certain proxy amounts used to set rates and the actual amounts. The variances resulting from the true-up were tracked in account 1562 for the period 2001 through April 30, 2006. For periods beginning May 1, 2006 the Board created account 1592 which primarily captures known changes in tax legislation and, unlike account 1562, has minimal scope for truing up amounts recorded.

In its AIC, HOBNI provided the following table listing the tax impacts of regulatory assets movements and the excess interest expense clawback and the remaining balance of the account 1562. [8]

Interest Clawback	$ 4,347,685
Bill 4 *(regulatory asset recoveries recorded in account 1590)*	$ 4,086,573
Proxy vs Entitlements & Other True-ups	$(2,841,943)
Balance applied for in account 1562	$ 5,592,315

In reports filed with the Board in April 2010, HOBNI reported a credit balance, or refund to customers, in account 1562 of $2,690,380 for the year 2009. In initial pre-filed evidence supporting the current application dated June 30, 2010, HOBNI requested disposition of a recovery from customers of $3,446,414.[9] In an update filed on September 30, 2010 the applicant altered its request to a recovery of $5,592,315, which includes interest forecast to December 31, 2010.[10]

Combined Proceeding EB-2008-0381

The Board currently is conducting a separate combined proceeding, *Account 1562 – Deferred Payments in Lieu of Taxes, EB-2008-0381* (the "Combined Proceeding") to determine how and when the deferred PILs 1562 balances should be disposed. The Board intends to consider the outcome of the Combined Proceeding to determine the appropriate method going forward to deal with the review and disposition of the balances in account 1562 for all remaining rate regulated electricity distributors.

[7] SIMPIL reconciliation which is an acronym for spreadsheet implementation model for payments-in-lieu of taxes
[8] AIC, pg.7
[9] Exh.9/Tab1/Sch.5.0/pg3 June 30, 2010
[10] Exh.9/Tab1/Sch.5.0/pg3 September 30, 2010

On December 18, 2009 the Board issued a decision in the Combined Proceeding and provided its views on how it will review the evidence.

> The Board agrees that the appropriate approach is a review of the account in terms of whether the distributors applied the methodology appropriately as the methodology existed at the time. The Board finds that it would be inappropriate to now change the methodology which was used in the past. This would only be appropriate if the Board had clearly signaled that the methodology itself would be subject to future revision on a retrospective basis. The Board made no such pronouncement. While the Board's methodology may not have been formally tested and adopted through a rates proceeding, the tools clearly were sanctioned by the Board and formed the basis on which distributors were expected to operate. It was reasonable to expect that any methodological changes would be prospective in their application.[11]
>
> The parties may well differ in their interpretations of the methodology but the Board will decide those questions on the basis of the facts and the underlying documents. The Board will not enter into an enquiry as to what the methodology should have been but rather, will determine, where necessary, what the methodology was and what the appropriate application of the methodology should have been.[12]

A settlement agreement filed in the Combined Proceeding was accepted by the Board on December 23, 2010.[13] [14] Two of the settled issues in the Combined Proceeding relate to the tax impact of changes in regulatory asset balances and the excess interest expense clawback. In the settlement agreement, the parties agreed that regulatory assets should be excluded from PILs calculations both when they were created, and when they were collected, regardless of the actual tax treatment accorded those amounts. Parties also agreed to maintain the interest clawback adjustment. HOBNI was not a party to this settlement agreement.

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[11] EB-2008-0381,Account 1562–Deferred Payments in Lieu of Taxes (PILs), combined proceeding, pg. 5-6
[12] Ibid, pg. 7
[13] December 6, 2010, K1.6 Board staff PILs compendium, K1.6, pg1-28
[14] EB-2008-0381, Decision and Procedural Order No. 9, December 23, 2009

In this proceeding, HOBNI has taken a different view of these two issues and the Board decided to hear the evidence that has been placed on the record.

> As noted in the October 19th letter, in which the Board decided to proceed with hearing that part of HOBNI's application dealing with this account 1562, the Board has not yet determined whether the circumstances in this proceeding are sufficiently different than the combined proceeding that has a docket number EB-2008-0381.
>
> After hearing the evidence, one of the decisions that this Panel will have to make is whether to proceed to dispose of this account at all, given that there is a combined proceeding under way that is intended to result in a common methodology for the remaining distributors to dispose of in their respective accounts.[15]

BOARD FINDINGS

In considering HOBNI's evidence for these two issues, the Board finds that there is sufficient evidence to make findings at this time. The Board finds that the approach described in the Board's decision in the Combined Proceeding is the appropriate approach in this case. The methodology as it existed from 2001 through April 30, 2006 will be used to determine how the evidence in this case has been applied to calculate the final balance in PILs account 1562.

The Board has decided that the balance in PILs account 1562 will not be cleared at this time. Rather, the Board addresses the two issues noted above, the tax impact of changes in regulatory asset balances and the excess interest expense clawback, within the scope of this proceeding. However, the Board withholds approval to dispose of the balance in account 1562 until after the Board issues its decision in the Combined Proceeding. At that time, HOBNI may file for disposition of PILs account 1562 in a manner that reflects the Board's findings on the remaining issues. Any such application must include and incorporate the Board's findings on the two issues that are the subject of this proceeding.

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[15] Tr. Vol. 1, December 6, 2010, pg.3

PILs Tax Impact of Changes in Regulatory Assets and Collections

The Board's deferral and variance accounts created for electricity distributors received the description of "regulatory assets" in the *Energy Pricing, Conservation and Supply Act, 2002, S.O. 2002, c.23 (Bill 210)*. In December 2003, the Minister of Energy issued a letter to set out a process by which distributors could proceed to recover their incurred costs associated with regulatory assets over a four year period. The Board decided to begin the recovery with an effective date of March 1, 2004 and that this recovery would be on an interim basis until final approval on the quantum of the costs was granted by the Board.

HOBNI applied, and received approval for, the first interim recovery installment in 2004 in accordance with the filing guidelines[16]. It applied again in 2005, and received approval, for the second interim installment. Board staff noted that HOBNI received final Board approval for disposition of regulatory assets in its 2006 rate application.[17]

In the Board staff submission, Board staff described how the change in regulatory assets impacts account 1562 and that if regulatory expenses were deducted on tax returns, these deductions would be negative entries in the SIMPIL reconciliation because they reduced net income for tax purposes. On the revenue side, recovery of regulatory assets resulted in an addition to income in the tax returns, and a positive entry in the SIMPIL reconciliation. Board staff explained that the Board's methodology to determine regulatory PILs taxes could not generate the correct result unless both sides of the regulatory asset equation are left in the reconciliation true-up to ratepayers or are excluded from this true-up reconciliation altogether.

Beginning in 2004, HOBNI recorded the interim recoveries of regulatory assets in account 1590 in accordance with the Board's instructions.[18] In response to Board staff interrogatory #63, HOBNI answered as follows:

> Hydro One Brampton excluded regulatory assets/liability movements from PILs calculations both when they were created, and when they were collected, regardless of the actual tax treatment used for those amounts. Hydro One Brampton accounted for these as items that are not trued up in the TaxRec3 tab of the SIMPIL models for each year from 2001 to 2005.

[16] December 6, 2010, K1.6, Board staff PILs compendium, pg44-53
[17] Ibid, pg54-55, 63-64, 76
[18] Ibid, ,pg40 ln21-28, pg 41 ln1-18

While HOBNI's PILs calculation excluded regulatory asset/liability movements, regulatory assets and liabilities were not excluded from the required SIMPIL true-up calculations. This resulted in an increase to the debit balance recorded in Account 1562 for which HOBNI is now seeking recovery from customers.

In its AIC, HOBNI stated that since the regulatory asset amounts recovered from customers were approved by the Board on an interim basis, those amounts should not be treated as changes in regulatory assets in the PILs true-up for 2004 and 2005. HOBNI interpreted the interim recovery as meaning there was doubt that it would be allowed to retain the full amount of the recoveries posted to account 1590 and that its tax returns disclosed the balances as tax reserves (provisions).[19] HOBNI noted that the Board approved its regulatory assets on a final basis on April 12, 2006 and that the final disposition approved for the regulatory assets continued beyond the PILs true-up period. Since HOBNI was unsure whether the regulatory assets would be recovered at that time, it submitted that it would be just and proper to include the true-up related to regulatory assets in the balance of account 1562.[20]

Board staff noted that in its audited financial statements HOBNI disclosed the recoveries as reductions in the regulatory asset balances and not as reserves. Board staff submitted that HOBNI should include the negative SIMPIL entries related to tax deductions of regulatory assets from 2001 to 2005 or remove the impact of the recovery of regulatory assets in its SIMPIL calculations and reconciliations for the tax years 2001 through 2005. Further, Board staff stated that the correct answer cannot be determined if both sides are not included or excluded in the same part of the SIMPIL true-up models.

VECC and Energy Probe agreed with Board staff's position.

SEC stated that if an Applicant took the tax deductions during the period 2001-2006, the account 1562 true-up calculation would have to reduce its taxable income by a similar amount. This calculation would increase the amount for the reconciliation between the PILs proxy and tax paid. SEC submitted that the methodology that HOBNI used was

[19] Ibid, pg38 ln13-28, pg39 ln1-28, pg40 ln1-17

[20] In November 2003, the government announced, in conjunction with the introduction of Bill 4, the *Ontario Energy Board Amendment Act, (Electricity Pricing), 2003*, that electricity distributors could start recovering Regulatory Assets in their rates, beginning March 1, 2004, over a four year period.

not only inconsistent with the Board's methodology, but also created asymmetrical treatment of the tax costs and benefits.

In its reply submission, HOBNI submitted that its interpretation and methodology are justified as stated in its AIC.

BOARD FINDINGS

On November 25, 2003, the government announced, in conjunction with the introduction of Bill 4, the *Ontario Energy Board Amendment Act, (Electricity Pricing), 2003*, that Local Electricity Distribution Companies could start recovering regulatory assets in their rates, beginning March 1, 2004, over a four-year period. On December 19, 2003, the Minister of Energy exercised his authority under s.79 of the Act[21] and issued letters to the Board and to electricity distributors allowing the Board to receive applications for recovery of prudently incurred regulatory assets.

HOBNI filed its application for the first installment of recovery in 2004. The Board approved the requested recovery in its decision EB-2004-0013 dated March 11, 2004. The second installment for HOBNI was approved in decision EB-2005-0008 on March 21, 2005. On April 12, 2006 in decision EB-2005-0377, the Board approved the final unrecovered balances of HOBNI's regulatory assets for collection over the remaining two years consistent with the four-year recovery period which began in March 2004.

While some degree of doubt about the recoverability of regulatory assets and liabilities may have existed in 2002, the government enacted legislation in late 2002[22] prescribing certain accounts as regulatory assets until the Board addressed the disposition. Subsequently, in December 2003, the Minister of Energy sent a letter to all distributors granting them approval to make rate applications to the Board with regard to the recovery of regulatory assets. The Board is of the view that the government provided considerable certainty about the future recovery of regulatory assets by these actions.

As described earlier in this Decision, the recovery of regulatory assets recorded in account 1590 was disclosed in HOBNI's tax returns as an increase in taxable income, whether by changes in tax reserves or provisions. The deferred expenses called

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[21] *Ontario Energy Board Act, 1998 S.O. 1998*, Chapter 15 Schedule B
[22] Bill 210 *Electricity Pricing, Conservation and Supply Act, 2002*

regulatory assets were deducted in HOBNI's tax returns. This resulted in symmetrical entries to tax returns related to regulatory assets.

Yet, when filing evidence in the current application, the Board notes that HOBNI revised its approach to reflect only one side of the equation. It is the Board's view that the activity in any given tax year should be viewed as part of the entire 2001-2006 period's series of tax activities and not as a year in isolation from the full period under examination. Deductions serve to reduce the tax otherwise payable and recoveries cause increases in taxable income, and thereby taxes. In order to arrive at a reasonable account balance which is fair to both the applicant and ratepayers, recoveries and deductions must be treated symmetrically for the purposes of the true-up calculations. In the Combined Proceeding, the settlement agreement approved by the Board excluded both recoveries and deductions from the determination of the balance in PILs account 1562. The Board approves the same approach for HOBNI.

When HOBNI submits its evidence under the Board's process that will result from the decision in the Combined Proceeding, HOBNI is directed to exclude entries for regulatory asset recoveries and deductions in the determination of the balance in account 1562.

Interest Expense Clawback

In its submission, Board staff explained that if a distributor deducted the higher actual interest expense in its tax returns it paid less tax. In determining distribution rates for the period 2001 to 2005, the Board adopted deemed capital structures and deemed interest rates based on the relative size of the distributors. In any given year there was a difference between the deemed interest expense included in distribution rates and the interest deducted in the corporate tax returns.

The SIMPIL excess interest clawback calculation resulted in recording in account 1562 the tax effect of the amount by which a distributor's actual interest expense was in excess of the deemed interest expense.[23] This clawback is a negative entry or deduction in the SIMPIL worksheets and results in a credit back to customers. This clawback feature was disclosed by the Board in application filing instructions in the fall of 2001. HOBNI agreed that the clawback has been a feature of the SIMPIL true-up

[23] For the purposes of this calculation, the deemed interest expense was based on a distributor's full return, even though the return was being phased in over three tranches.

methodology but stated that it created its actual capital structure before the Board issued its filing guidelines.

In its SIMPIL filings over the years, HOBNI included the interest clawback. However, it removed the effect of the clawback on account 1562 when it updated its evidence in the current proceeding.

In its reply argument in the current proceeding, HOBNI stated that:

> Brampton raised its concerns regarding the interest clawback as an intervenor in the combined PILs proceeding EB-2008-0381, on November 20, 2009, and updated the Account 1562 balance subsequently in this disposition filing.[24]

In its evidence, HOBNI listed four principal reasons why it believes that the clawback is not just and reasonable.

a. The capital structure of 55% debt and 45% equity was created in a manner consistent with other subsidiaries of the parent and consistent with the public prospectus released by the parent. Unlike many other distributors, HOBNI is part of a larger family of companies.
b. The Company is unique in that push-down accounting was used to record $60 million of goodwill, and the debt and equity amounts were based on balance sheet values including goodwill. Debt values for rate-making purposes rarely equate to balance sheet values.
c. The Company experienced significant growth during the years the clawback was calculated, thereby requiring debt levels to rise to fund a portion of the capital investment required.
d. There was no customer impact as a result of the capital structure adopted by the Company: the distribution rates paid by customers were not affected.

Board staff noted that HOBNI filed an analysis that shows goodwill of $60,060,000 recorded on its balance sheet after Hydro One Inc. acquired HOBNI in 2001. Debt increased from $114,579,000 at December 31, 2000 to $142,227,000 by December 31,

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[24] Hydro One Brampton Reply argument, pg20

2001. From 2001 through 2009 this debt remained almost unchanged. [25] Shareholder's equity increased from $122,941,000 at the end of 2001 to $142,972,000 by December 31, 2001. The value of goodwill was included in the determination of the actual debt and equity amounts as stated by HOBNI.

Board staff submitted that HOBNI had not adequately demonstrated why the Board should completely abandon its long-held policy reflected in the interest clawback adjustment. However, Board staff stated that it would not oppose the Board considering some reduction of the clawback adjustment amount if HOBNI had demonstrated that the majority of the excess interest was caused by the higher debt level to fund the growth of its customers.

VECC and Energy Probe agreed with Board staff's position.

In its submission, SEC stated that in the Combined Proceeding, there was a debate about whether the Board should implement the rule that it had put in place in 2001 through 2006 or should determine the most fair and reasonable method of truing up PILs over that period. SEC noted that in the Combined Proceeding the Board found that it would be inappropriate to change the methodology which was used in the past. SEC submitted that since the interest clawback was part of the methodology, the principle stated that the clawback must apply.

SEC also noted that in the period of account 1562, the Applicant had collected $39,660,297 from ratepayers to pay PILs and the actual taxes paid for the same period were $32,468,553. The Applicant had collected $7,211,744 more in rates for PILs than it had paid in taxes. But SEC stated that the Applicant argued it should collect a further $5.6 million from ratepayers by retroactively adjusting the methodology during that period. SEC submitted that the Applicant's argument is completely unsustainable and the Board should reject it completely.

In its reply submission, HOBNI submitted that the interest clawback was not just and reasonable for two reasons. The first reason was that HOBNI's interest clawback issue pre-dates the PILs 1562 methodology. The second reason was that its distribution rates for the period from 2001 to 2005 were established based on the static 1999 rate base values. HOBNI explained that the deemed threshold interest expense was inadequate to fund its higher rate base and capital structure and it would be appropriate and

[25] December 6, 2010, K 1.6, Board staff PILs compendium, pg119

reasonable for the Board to make an exception to permit HOBNI to adjust the interest expense thresholds for true-up calculations.

BOARD FINDINGS

The Board's interest expense clawback methodology effectively deprives the distributor of the tax benefits associated with incurring higher interest expense as a deduction in its tax returns. The threshold set by the Board was equivalent to the amount of interest expense to be included in rates once the distributor had reached full capitalization consistent with the deemed capital structure. Any interest expense in excess of this threshold became subject to the Board's excess interest clawback adjustment. HOBNI used the lower deemed interest expense in its application for 2002 PILs to be included in rates rather than the higher actual interest expense.

In its reply argument as referred to above, HOBNI noted that it had raised its concerns regarding the interest clawback as an intervenor in the Combined Proceeding, on November 20, 2009. HOBNI updated the account 1562 balance subsequently in this disposition filing. However, HOBNI did not submit evidence that it had filed an objection to the Board's interest clawback methodology while it was in force during the period 2001 through 2005. The Board is not aware of any distributor having filed an objection to the Board's interest clawback methodology during that same period.

In addition, the Board notes that HOBNI recorded goodwill of $60,060,000 after Hydro One Inc. acquired Brampton Hydro in 2001. As noted above, the capital structure of 55% debt and 45% equity was adjusted to reflect the addition of goodwill. From HOBNI's reply to Board staff's interrogatory #65(e), the balance sheet information from 1999 through 2009 shows how debt and equity changed in response to the goodwill recorded in 2001. The balance sheet analysis also discloses that the debt levels, once created after goodwill was recorded in 2001, changed very little through December 31, 2005. However, shareholder's equity increased during this same period by $20,031,000 from $122,941,000 to $142,972,000. Net fixed assets grew by $17,591,000 from $197,287,000 to $214,878,000. While the company may have experienced significant growth in its service area during those years, it does not appear from the balance sheet analysis that additional debt was raised to finance this customer-driven growth.

HOBNI stated that there was no customer impact as a result of the capital structure adopted by the company since the distribution rates paid by customers were not

affected. Goodwill was not included in rate base in its 2002 application, and consequently, the deemed debt and equity levels used in that application were correspondingly lower.

The Board's SIMPIL methodology created in the 2001-2002 rate periods did not identify causes of debt and related interest expense. The methodology compares the interest expense deducted in the preparation of the tax return for a given tax year with the deemed interest expense for the same tax year. The difference between the two sources is the excess interest expense subject to the clawback mechanism which results in a refund to customers.

Earlier in this Decision, the Board stated that it finds that the approach described in the Board's decision in the Combined Proceeding is the appropriate approach in this case. Had HOBNI's evidence demonstrated that debt was increased to finance the growth in net fixed assets as it stated was necessary, the Board may have been able to justify a connection. However, from HOBNI's own evidence it appears that financing was provided by operational cash flow reflected in increasing shareholder's equity, and not by raising additional debt.

The Board finds that the excess interest clawback adjustment should be applied in the SIMPIL reconciliations submitted by HOBNI. Consequently, HOBNI will include the excess interest tax deduction as a reconciling item that trues-up according to the established methodology in the SIMPIL worksheets.

Disposition of Deferred PILs Account 1562

HOBNI is requesting to dispose the account 1562 over a two year period. Board staff submitted that in the event there is a reduction in the total balance, the rate rider associated with the residual balance should be derived for only one year.

Energy Probe agreed with Board staff's proposal for the recovery period depending on the balance of account 1562.

HOBNI responded that based on its current submission the disposition period should be two years. However, if the Board approved a lower amount for regulatory asset recovery, HOBNI submitted that one-year disposition period might be appropriate.

BOARD FINDINGS

The Board has made findings on the two PILs 1562 issues raised in this proceeding. Having described how these issues should be reflected in revised evidence yet to be filed by HOBNI, the Board must consider the implications of the Board's Combined Proceeding which is still before the Board.

As noted earlier in this Decision, the Board will not order disposition of the balance in HOBNI's PILs account 1562 at this time. After the Board issues its decision in the Combined Proceeding, and HOBNI receives instructions to file an application consistent with the directions to be given by the Board in the Combined Proceeding, the Board will approve a final balance to be cleared.

HOBNI is directed to file revised calculations as part of the draft Rate Order in this proceeding that show the results of excluding the regulatory assets and recoveries, and including the interest clawback adjustment in calculating the balance in account 1562. HOBNI should calculate interest carrying charges to December 31, 2010. While the Board will not be disposing of account 1562 in this proceeding, the Board would be assisted by parties' comments on the accuracy of the revised calculations as part of the comment period on the draft Rate Order. HOBNI is directed to file live EXCEL versions of the SIMPIL worksheets for all applicable years.

SMART METERS

HOBNI is requesting the approval of its smart meter capital and OM&A costs on a final basis to the end of December, 2009, a 12 month Disposition Rate Rider of $0.54/month to recover the residual balance in the smart meter variance accounts, and an adjustment to its Smart Meter Funding Adder from $1.00/month to $1.01/month going forward to fund the remaining portion of its smart meter rollout.

Final Review of capital and OM&A costs to December 31, 2009

HOBNI has documented that its capital and OM&A costs per smart meter net of depreciation for meters installed from 2006 to 2009 are $164.87 and $21.69 respectively. On a combined basis, the cost per installed smart meter is $186.56.

Board staff noted that in the Board's decision in the combined smart meter proceeding (EB-2007-0063), the total capital and OM&A costs per installed smart meter for HOBNI was $148.04. HOBNI explained that the increase was due to higher capital costs for the small industrial/commercial meters, development IT costs and maintenance costs associated with failed meter bases that arose subsequent to the combined smart meter proceeding.

Board staff submitted that it had no issue with HOBNI's documented costs for smart meters installed up to 2009. HOBNI had recorded all the costs for smart meters in the smart meter deferral and variance accounts (1555 and 1556). Board staff noted the smart meter costs incurred to the end of December 2009 had been audited and the corresponding capital costs have been included in 2011 rate base.

Energy Probe, SEC, and VECC made no submissions on the disposition of smart meters capital and OM&A costs.

BOARD FINDINGS

The Board notes that the costs related to HOBNI's smart meter program for the period of 2006 to 2009 are higher than the amounts identified in the combined smart meter proceeding. However, the Board finds that HOBNI has provided evidence to justify the increase. The Board accepts the costs as having been prudently incurred and approves them.

Smart Meter Disposition Rate Rider

HOBNI is requesting a 12 month Disposition Rate Rider of $0.54/month to recover the remaining revenue requirement for the 2007 to 2009 period of smart meters installed up to the end of 2009. The Disposition Rate Rider takes into account the actual revenue collected to the end of 2009 through the Smart Meter Funding Adder. The net result is a recovery amount of $851,845 that would be recovered over the January 1, 2011 to December 31, 2011 period.

Board staff noted that the smart meter costs incurred to the end of December 2009 had been audited and had no concerns on the proposed Smart Meter Disposition Rate Rider.

Energy Probe agreed with the proposed Smart Meter Disposition Rate Rider.

VECC noted that HOBNI's proposed allocation of the disposition rate rider is not consistent with the cost allocation approach as proposed by PowerStream Inc and accepted in the Board's decision (EB-2010-0209). VECC submitted that a class-specific allocation should be used in determining the disposition rate riders.

BOARD FINDINGS

The Board accepts the Applicant's recovery amount over a recovery period of May 1, 2011 to December 31, 2011. The Board finds that the Smart Meter Disposition Rate Rider should be recovered from all metered customers and directs HOBNI to recalculate its disposition rate rider based on an eight month period.

The Board notes that the Board's decision in PowerStream's smart meter application did not require class specific allocations. The Board does not find any compelling reason to require this to be done in this case either.

Smart Meter Funding Adder ("SMFA")

HOBNI requested an ongoing SMFA of $1.01/month to cover additional investments in smart meters in 2010 and 2011 as well as the revenue requirement for 2010 for the smart meters installed up to 2009.

Board staff stated that the SMFA was intended to provide the funding for the deployment of smart meters. Since HOBNI had installed 93.7% of the total number of smart meters and its smart meter deployment would be completed in 2011, Board staff submitted that the SMFA should be discontinued.

Board staff also stated that HOBNI might consider filing a smart meter application once its 2011 audited financial statements are available. This smart meter application would allow HOBNI to recover the proxy revenue requirement for the remaining smart meters and to mitigate its costs pressure before the next rebasing application.

Energy Probe disagreed with Board staff's proposal with discontinuing the SMFA. Energy Probe stated that the continuation of the funding adder would result in regulatory

efficiencies and the prudence review of the balances of the Smart Meters could be dealt with as part of the next cost of service rebasing application.

VECC submitted that the SMFA should be calculated on a class-specific basis by using the capital costs as the allocator of the forecasted revenue requirement.

HOBNI responded that it would continue to require a SMFA until the smart meter program is completed and final disposition approved by the Board. HOBNI explained that although 93.7% of smart meters had been installed, it plans to spend an additional $5.7 million in smart meter capital costs. The funding would also ensure that the ongoing cash flow to support the project is available. HOBNI stated that it would seek the final disposition of the remaining smart meters as part of its next cost of service application in 2015, rather than during a separate interim proceeding.

BOARD FINDINGS

Since the deployment of smart meters on a province-wide basis is now nearing completion, the Board expects distributors to file for a final prudence review at the earliest possible opportunity following the availability of audited costs. The Board expects HOBNI to file an application with the Board seeking final approval for the remaining smart meter related costs. In the interim, the Board will approve a SMFA of $1.52 per metered customer per month from May 1, 2011 to December 31, 2011. While this is higher than the amount proposed by HOBNI of $1.01, it provides for adequate funding over a shorter rate implementation period determined later in this Decision. The SMFA of $1.52 per metered customer per month will be reflected in HOBNI's Tariff of Rates and Charges, and shall cease on December 31, 2011. HOBNI's variance accounts for smart meter program implementation costs, previously authorized by the Board, shall be continued.

Stranded Meters

HOBNI is proposing to retain the stranded meter costs in rate base. Board staff submitted that HOBNI will receive rate base treatment on its smart meters that have replaced the "stranded" meters. As a result, it may no longer be appropriate for the distributor to receive concurrent rate base treatment for stranded meters that are no longer used and useful. The application indicates that HOBNI has installed 125,192[26]

[26] Exh.9/Tab3/Sch.1.1/pg.1

smart meters as at year-end 2009 representing 94.4% of all RPP-eligible consumers to the end of 2010. In addition, $18,113,681[27] for smart meter capital costs requested for disposition in Account 1555 was requested for inclusion in rate base.

Board staff also submitted that the total estimated stranded costs of $2,275,483.47 as of December 31, 2011 could be allowed to be recovered through a separate rate rider for a two year period (or four year period if the bill impacts were too high). Board staff stated that the total estimated stranded costs should be removed from rate base and tracked in "Sub-account Stranded Meter Costs" of Account 1555. The revenue collected from the rate rider should be recorded in this sub-account to draw down the balance in the sub-account. These amounts would be submitted for review and disposition in HOBNI's next cost of service application.

Energy Probe supported Board staff's proposal that the stranded meters are no longer used and useful when the new smart meters are also included in rate base. Energy Probe agreed with transferring the net book value of the stranded meters from rate base to a separate account as proposed by Board staff and submitted that the proposed recovery period, taking into account the overall bill impacts, should be as short as possible.

In its reply submission, HOBNI submitted that it is appropriate to retain its stranded meters in rate base and have concurrent rate base treatment for smart meters. HOBNI explained that it invested in conventional meters with the expectation of earning a regulatory return on those meters. Further, it was required to remove the conventional meters by government legislation. In regards to the reference to the "used and useful" rule, HOBNI submitted that it is not relevant in this case given that the stranded meters have been included in rate base for several years. HOBNI further stated that it had followed the Board's *Smart Meter Funding and Cost Recovery Guideline (G-2008-0002)* to include its stranded meters in rate base.

HOBNI concluded that in its decision on the combined proceeding (EB-2007-0063) the Board had two options to deal with stranded meters. The first was to include them in rate base. The second was to write off their carrying value and record this amount in a deferral account with interest charged to the account to reflect financing costs. HOBNI

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[27] Exh.9/Tab3/Sch.2 Table 1(Gross Capital in Services of $19,882,909 less Accumulated Depreciation of $1,769,228)

submitted that since the Board had adopted the rate base model instead of the deferral account model, the stranded meters should also be permitted to earn a return.

BOARD FINDINGS

The Board does not agree with HOBNI's proposal to retain the stranded meter costs in rate base where it continues to receive a return on these meters. The reasons are outlined below.

The approach taken by the Board in the combined smart meter proceeding (EB-2007-0063) decision of August 8, 2007, was to defer any final decision regarding the treatment of stranded meters. At the time, neither the Board nor the 13 electricity distributors which were parties to that proceeding had sufficient information on this transitional meter issue to establish an acceptable approach to address the rate recovery of stranded meters. Accordingly, the Board accepted a proposal to leave the stranded meters in rate base. Specifically, the 2007 decision stated the following:

> "Many of the utilities suggested that at the present time, the stranded costs associated with existing meters should stay in rate base. The Board accepts this proposition.
>
> Utilities can, if they choose, bring forward applications for the recovery of stranded costs in their 2008 rates. <u>However, there are several reasons why the Board is deferring the decision at this time.</u> First, the roll-out of smart meters will occur over four years. Second, the undepreciated amounts are unknown. Finally, the cost savings are unknown, as are the rate impacts. [Emphasis added]
>
> The Board has determined that all utilities should continue to track the costs associated with stranded meters."

It is clear to the Board that leaving stranded meters in rate base was intended to be an interim measure and the Board provided reasons for deferring recovery in its decision. In the past, distributors have sought and received recovery of their stranded meters including their removal from rate base.

HOBNI has asserted that it invested in conventional meters with the expectation of earning an ongoing regulatory return on those meters and that it was required to remove the conventional meters by government legislation. Essentially, it argued that it should continue to receive a return, as it had no control over the removal of the conventional meters.

The Board does not agree with this simplistic assessment. The Board's view is that government regulation specifies that distributors may recover stranded meter costs subject to certain conditions being met. In 2007, Ontario Regulation 441/07 came into force which amended Ontario Regulation 426/06 (Smart Meters: Cost Recovery) by adding a new section that specifically addressed the recovery of stranded costs associated with the smart metering initiative. The section states as follows: "Subject to Board order, distributors may recover the costs associated with meters owned before, on or after January 1, 2006 being replaced because of the smart metering initiative if, (a) the meter being replaced was not acquired in contravention of section 53.18 of the *Electricity Act, 1998*; and (b) the meter is replaced with a smart meter authorized for installation under the *Electricity Act, 1998*." [Emphasis added]

With respect to the Board's Guideline: Smart Meters Funding and Cost Recovery (G-2008-0002), which HOBNI has referenced for its stranded meter treatment, it should be noted that the Guideline provides two options to distributors regarding the accounting treatment for stranded meters. The two options in the Guideline for the stranded meters are to leave them in rate base (i.e. Account 1860) or record them in "Sub-account Stranded Meter Costs" of Account 1555.

Accounting guidance in the December 2010 Accounting Procedures Handbook FAQs (Q and A #15) provides that the 2011 cost of service rate-setting process may address the manner in which distributors plan to recover costs associated with stranded meters. In the Board's view, the time to address the recovery of stranded meters is optimal in the 2011 cost of service applications process as most distributors have completed or nearly completed their installation of smart meters and have included a significant portion of these costs in rate base. In addition, the accounting guidance provided in states that stranded meter costs which are to be considered for recovery would be reviewed regardless of which account the stranded meter costs are recorded, and that only the net book value of the stranded meters will be allowed for recovery. Accordingly, the stranded meter costs for recovery purposes will comprise the gross

costs of the stranded meters, less any capital contributions, less the accumulated depreciation and less any proceeds from the disposition of the meters.

Board staff submitted that HOBNI would receive a concurrent return on two sets of meters (stranded conventional and smart) and that the inclusion of stranded meters in rate base might be inappropriate given that the distributor would receive rate base treatment for stranded meters that are no longer used and useful. In its application, HOBNI is clearing $18,113,681 for smart meter costs as of December 31, 2009 in Account 1555 and has included this amount in rate base. This represents almost full deployment of smart meters at 94% of all eligible RPP customers, which generally represents the number of customers that are eligible for smart meters. In the Board's view, the continued inclusion of stranded meters in rate base while at the same time allowing smart meters in rate base would constitute a double counting of assets in rate base.

The Board directs HOBNI to remove the total estimated stranded costs of $2,275,483.47 as of December 31, 2011, or a revised amount in accordance with the above-noted accounting guidance, from rate base and recalculate the impact on its revenue requirement. In addition, HOBNI is directed to establish separate rate riders for the applicable customer classes to recover the amount in its draft Rate Order. The length of the recovery period shall be 20 months to coincide with HOBNI's new distribution rate year.

Upon approval of the final Rate Order, the total estimated stranded costs should be tracked in “Sub-account Stranded Meter Costs” of Account 1555. The associated recoveries from the separate rate riders should be recorded in this sub-account to reduce the balance in the sub-account. Given the fact that HOBNI had not completed 100% of its smart meter deployment at the time of this application, the Board will require that the approved 2011 estimate for the stranded meter costs be trued-up to actual stranded meter costs when the installation of all smart meters is completed. An adjusting entry shall be recorded for this adjustment in the sub-account and the revised balance (net of recoveries) shall be submitted for review in HOBNI's next cost of service application.

LOST REVENUE ADJUSTMENT MECHANISM (“LRAM”) / SHARED SAVING MECHANISM (“SSM”)

HOBNI is seeking LRAM and SSM recovery of $2,395,597 ($1,850,549 for LRAM, $86,609 for carrying charges and $458,438 for SSM), to be recovered over two years.

Board staff submitted that HOBNI’s application for LRAM and SSM recovery is consistent with the Board’s Guidelines[28].

VECC supported HOBNI’s SSM claim; however it did not support the LRAM claim related to HOBNI’s third tranche programs. In particular, the program related to the 2006 and 2007 Every Kilowatt Counts (“EKC”) used OPA 2009 results for input assumptions, which VECC noted was incorrect. In reference to the Board’s decision on Horizon’s CDM application (EB-2009-0158/EB-2009-0192), the Board required Horizon to update its input assumptions using the most current input assumptions adopted by the Board. VECC submitted that HOBNI should be using the OPA 2010 results for input assumptions.

HOBNI noted that the data used in its LRAM calculation for 2006 and 2007 EKC were from an evaluation of those specific programs commissioned by the OPA. HOBNI also highlighted that it believed the Board’s decision on Horizon’s CDM application addressed the issue on whether the most current datasets for LRAM purposes applied to programs offered before 2007. It was not about the difference between the results from a program-specific evaluation and the most current ‘generic’ assumptions used.

BOARD FINDINGS

The Board approves HOBNI’s request to recovery an LRAM of $1,937,158, inclusive of carrying charges, and an SSM of $458,438.

The Board continues to endorse the principle of LRAM, which is that distributors are to be kept whole for revenue that they have forgone as a direct consequence of implementing their CDM programs.

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[28] Guidelines for Electricity Distributor Conservation and Demand Management, issued on March 28, 2008.

The Board is of the view that the most current OPA Measures and Assumptions List, as updated by the OPA from time to time, represents the best estimate of losses associated with a distributor's CDM programs. The Board finds that HOBNI's calculation of the LRAM Claim related to its 2006 and 2007 EKC programs is appropriate. The Board notes that the use of OPA-verified results in the calculation of the lost revenue related to third-tranche CDM programs is appropriate.

EFFECTIVE DATE

HOBNI applied for rates effective January 1, 2011. At the oral hearing, the Board declared HOBNI's current rates interim, which allows for an effective date as early as January 1, 2011.

Both VECC and SEC made submissions on the appropriateness of the rate year and the effective date of the new distribution rates.

VECC stated that HOBNI did not provide the required evidence to support an alignment of the rate year with the fiscal year as outlined in the Board's letter issued on April 15, 2010 and as asked though the interrogatory process. As a result, the Board should deny HOBNI's request for an alignment of its rate year with its fiscal year. However, should the Board decide to grant HOBNI's request for a January 1, 2011 rate year, VECC submitted that the effective date should be March 1, 2011 in part because HOBNI did not file its application on a timely basis for a January 1, 2011 effective date but did file its application two months earlier than the Board's deadline of August 27, 2010 for distributors seeking a May 1, 2011 rate year.

SEC supported the approval of rate and fiscal year alignment. SEC supported a March 1, 2011 effective date for the same reasons as those submitted by VECC. However, SEC suggested that given the revenue sufficiency of the application that HOBNI be directed to provide customers with a one-time payment of the sufficiency arising from January 1 to the date of implementation.

HOBNI responded that the rates should be set to allow for recovery of the full 2011 revenue requirement over the remaining months in 2011.

BOARD FINDINGS

The Board approves HOBNI's alignment of rate and fiscal year. HOBNI's new rates will be effective January 1, 2011. The Board has also determined that the implementation date will be May 1, 2011. The Board notes that while there is an overall revenue sufficiency that arises out of this Decision, this may not be the case within all rate classes. The Board orders HOBNI to dispose of any class specific sufficiency or deficiency arising from this Decision for the period January 1, 2011 to the implementation date. Accordingly, HOBNI is directed to calculate class specific rate riders that would either refund or recover from customers the stub period amount over a period of 8 months. HOBNI should also provide the detailed calculations of the rate riders in its draft Rate Order. The current interim rates are in effect until the Board approves the final Rate Order.

LATE PAYMENT PENALTY LITIGATION COST

In its application, HOBNI requested the recovery of a one time expense of $447,111.18 related to the late payment penalty ("LPP") costs and damages resulting from a court settlement that addressed litigation against many of the former municipal electricity utilities in Ontario.

On March 1, 2011, HOBNI filed its rate riders as outlined in the LPP Decision. However HOBNI also filed a separate letter on March 1, 2011, withdrawing its request to recover the LPP costs from its customers. The Board grants this request.

IMPLEMENTATION

The Board has made findings in this Decision which change the 2011 revenue requirement and therefore change the distribution rates from those proposed by HOBNI. In filing its draft Rate Order, it is the Board's expectation that HOBNI will not use a calculation of the revised revenue sufficiency to reconcile the new distribution rates with the Board's findings in this Decision. Rather, the Board expects HOBNI to file detailed supporting material, including all relevant calculations showing the impact of this Decision on HOBNI's 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.

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

1. HOBNI 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 **7 days** of the date of the issuance of this Decision. The draft Rate Order shall also include customer rate impacts and detailed supporting information showing the calculation of the final rates including the Revenue Requirement Work Form in Microsoft Excel format.

2. Intervenors shall file any comments on the draft Rate Order with the Board and forward to HOBNI within **7 days** of the date of filing of the draft Rate Order.

3. HOBNI shall file with the Board and forward to intervenors responses to any comments on its draft Rate Order within **4 days** of the date of receipt of intervenor comments.

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*. The Board will determine eligibility for costs in accordance with its *Practice Direction on Cost Awards*. 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.

1. Intervenors shall file with the Board and forward to HOBNI their respective cost claims within **7 days** from the date of issuance of the final Rate Order.

2. HOBNI shall file with the Board and forward to intervenors any objections to the claimed costs within **21 days** from the date of issuance of the final Rate Order.

3. Intervenors shall file with the Board and forward to HOBNI any responses to any objections for cost claims within **28 days** of the date of issuance of the final Rate Order.

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

All filings with the Board must quote the file number EB-2010-0132, and be made through the Board's web portal at www.errr.ontarioenergyboard.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. Parties should use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at www.ontarioenergyboard.ca. If the web portal is not available, parties may e-mail their documents to the attention of the Board Secretary at BoardSec@ontarioenergyboard.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*.

DATED at Toronto, April 4, 2011

ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary