

**Ontario Energy
Board**

**Commission de l'énergie
de l'Ontario**



EB-2007-0681

IN THE MATTER OF AN APPLICATION BY:

HYDRO ONE NETWORKS INC.

2008 RATES

DECISION WITH REASONS

December 18, 2008

EB-2007-0681

IN THE MATTER OF the *Ontario Energy Board Act, 1998*,
S.O. 1998, c.15;

AND IN THE MATTER OF an Application by Hydro One
Networks Inc. for an order or orders approving or fixing just
and reasonable rates and other charges for the distribution
of electricity commencing May 1, 2008.

BEFORE: Gordon Kaiser
Vice Chair and Presiding Member

Paul Sommerville
Member

Paul Vlahos
Member

DECISION WITH REASONS

DECEMBER 18, 2008

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1. Introduction

The Application

Hydro One Networks Inc. (“Hydro One”, or “the Company”) filed an application dated December 18, 2007 with the Ontario Energy Board (the “Board”) under section 78 of the *Ontario Energy Board Act, 1998*; S.O. c.15, Schedule B, for an order or orders approving or fixing just and reasonable rates for the distribution, of electricity effective May 1, 2008. The Board assigned file number EB-2007-0681 to the Application. Hydro One is one of over 80 electricity distributors in Ontario that are regulated by the Board. In 2006, the Board announced the establishment of a multi-year electricity distribution rate-setting plan for the years 2007 – 2010. Under that plan, all electricity distributors are to have rates set based on a cost of service rate filing in one of 2008, 2009 or 2010. Accordingly, Hydro One filed a cost of service application based on 2008 as the forward test year.

Appendix A contains details regarding the procedural aspects of the rates Application, including a list of witnesses and a list of participants.

The Settlement Proposal

On June 3, 2008, a Settlement Proposal was filed with the Board. A copy of the Settlement Proposal, is attached as Appendix B.

Of the 49 issues on the Issues List, the Settlement Proposal includes the complete settlement of 17 issues and indicated that parties would not address these issues at the hearing. There were 6 issues for which there was a partial settlement, and the parties were unable to reach agreement on the remaining 26 issues.

Below is a list of issues which are presented in the Settlement Proposal as having been completely settled. The Board accepts the cost consequences of the Settlement Proposal and will not review these issues in this Decision.

- Issue 1.3 Are the Affiliate Service Agreements appropriate?
- Issue 1.4 Are Hydro One's Economic and Business Planning Assumptions for 2008 appropriate?
- Issue 1.6 Is service quality on the OEB specified performance indicators acceptable?
- Issue 1.7 Are the proposed Distribution Loss Factors appropriate?
- Issue 2.1 Is the proposed Capital Structure and Rate of Return on Equity for Hydro One's distribution business appropriate?
- Issue 2.2 Are Hydro One's proposed costs and mix for its short and long-term debt for the 2008 test year appropriate?
- Issue 3.5 Is the proposed E-factor methodology and adjustment as part of the distribution overhead capitalization appropriate?
- Issue 3.7 Is Hydro One's depreciation expense appropriate?
- Issue 3.8 Are the amounts proposed for capital and property taxes appropriate?
- Issue 3.9 Is the amount proposed for income taxes, including the methodology, appropriate?
- Issue 3.11 Is the proposed spending on loss reduction efforts appropriate?
- Issue 4.8 Does the Asset Condition Assessment information adequately address the condition of the distribution system assets and support the OMA and Capital expenditures for 2008?
- Issue 4.9 Are the proposed capital expenditures to reduce electricity system losses appropriate?
- Issue 5.1 Is the calculation of the proposed revenue requirement for 2008 appropriate?
- Issue 5.2 Is the proposed amount for 2008 External Revenues, including the methodology used to cost and price these services, appropriate?
- Issue 7.9 Are the proposed Retail Transmission Service Rates appropriate?
- Issue 8.4 Is the treatment of stranded meter costs appropriate?

Interim Order of February 15, 2008

By way of letters dated December 20, 2007 and December 21, 2007, Hydro One filed two requests with the Board for the continuation, on an interim rates basis, of the existing Regulatory Assets Phase 2 - rate riders and the existing Time of Use rates until

such time as new distribution rates are implemented in this Application. The Board approved Hydro One's request in an oral decision on February 15, 2008 during Issues Day (see transcript).

Interim Rate Order of April 11, 2008

By way of a letter dated February 27, 2008 Hydro One requested that its existing 2007 rates for the distribution of electricity approved under proceeding EB-2007-0542, be declared interim effective May 1, 2008. An Interim Rate Order approving Hydro One's request was issued on April 11, 2008 and is attached as Appendix C to this Decision.

Non-settled Issues

This Decision with Reasons will address the non-settled issues under the following chapters:

- Load Forecast
- Conservation and Demand Management
- Operations, Maintenance and Administration
- Capital Expenditures and Rate Base
- Regulatory Treatment of Smart Meters
- Harmonization, Cost Allocation and Rate Design
- Deferral and Variance Accounts

The last chapter deals with implementation matters.

Copies of the evidence, exhibits, arguments, transcripts, and letters of comment filed in the proceeding are available for review at the Board's offices.

The Board considered the full record of the proceeding but has summarized the record only to the extent necessary to provide context to its findings.

Confidentiality

During the proceeding, the Company requested confidential treatment for three documents:

- 1) J2.5 – the CN Utility Study
- 2) J3.3 – Acquisition Financial Model
- 3) J3.10 – Quarterly Management Reports

The Schools Energy Coalition (“SEC”) agreed that Exhibit J3.3 should be treated confidentially. However, SEC argued that the other two documents should not be accorded confidential treatment. The Vulnerable Energy Consumers Coalition (“VECC”) adopted SEC’s submissions with respect to Exhibits J2.5 and J3.10.

The Board has determined that Hydro One would be commercially disadvantaged if its acquisition financial model came into the public domain. The Board has not and will not order the production of the Acquisition Financial Model. It will be treated confidentially.

In addition, the Board’s decision does not require the production of the other two documents. However, the Board does wish to make the following comments.

The claim for confidentiality for the CN Utility Study is based on the proposition that it contains proprietary information that the consulting firm itself generated for purposes of marketing its services. Even in such circumstances, where the study was not commissioned by Hydro One, the Company is still obligated to make such vendors aware that any reports or studies the Company purchases may be used or compelled as evidence, in whole or in part, in its regulatory proceedings. Determining whether a consultant’s report or study should be produced, in whole or in part, on the public record in a regulatory proceeding needs to be assessed on a case-by-case basis. Generally, if an expert’s study or report forms the basis on which the Company has made strategic

or operational decisions, it becomes probative evidence for the parties and the Board, and it is likely that the Board would compel production on the public record. The Board has established practices by which parties to proceedings can access confidential materials, provided they execute an undertaking in the form approved by the Board. This process is not to be confused with having the materials placed on the public record, where anyone can examine them.

The Board is mindful of Hydro One's status as a reporting issuer subject to regulation by the Ontario Securities Commission respecting public disclosure of Quarterly Management Reports. However, this does not absolve the company in certain circumstances from having to produce on the public record such reports, with the leave of or by order of the Board. The circumstances will indeed be exceptional and where the information is critical to the determination of a matter and cannot otherwise be reasonably adduced from other direct or indirect information in the examination process. Again, the matter is case and issue specific.

As for whether non-lawyers should also be receiving the confidential information, consideration of this matter should also be case specific. If the Company has any concerns in that regard in a specific case, it is expected that it would raise them at that time.

2. Load Forecast

In developing the load forecast for 2008 rates, the Company reflected the provincial Conservation & Demand Management (“CDM”) target of 1,350MW by 2007 and the Ontario Power Authority’s (“OPA”) forecast incremental CDM savings for 2008. To be consistent with the Board’s findings in the EB-2006-0501 Decision dealing with 2007 and 2008 transmission rates, the 2007 provincial target of 1,350MW incorporated a reduction of 350MW to account for natural conservation, for a net 1,000 MW CDM-driven reduction. For 2008, the Company added its estimated share of the 0.8 TWh of OPA’s incremental CDM forecast. The MW (peak) adjustments were converted into GWh (energy) adjustments based on assumptions on load factors of the Company’s retail customers and embedded distributor customers.

VECC referred to the results and data in the June 2008 report of the OPA’s Chief Energy Conservation Officer’s and argued that the CDM adjustment to the Company’s energy forecast for 2007 should be calculated using 800MW of demand reduction province-wide due to CDM, rather than the 1,000 value used by the Company. VECC’s position was supported by the Association of Major Power Consumers in Ontario (“AMPCO”), the Consumers Council of Canada (“CCC”) and SEC.

In reply, Hydro One noted that the CDM adjustment to its 2007 energy forecast is not based on 1,000 MW as noted by VECC, because the load impact of demand management programs on energy is assumed to be zero. In fact, Hydro One noted, the CDM adjustment to its energy forecast for 2007 is already based on about 500 MW which is 1,000 MW of the load impact of all demand management programs.

By comparing the forecast and actual values of load for 2006 and 2007, AMPCO noted that the Company’s actual load has been at about the same levels as its forecast before adjusting for the impact of CDM. AMPCO suggested that the explanation might be a) Hydro One supplied incorrect data, b) the weather normalization is flawed, c) the pre-CDM forecast actually incorporates CDM results, or d) CDM programs are totally ineffective or are being cancelled by unpredicted load growth.

Hydro One noted that AMPCO has misunderstood the evidence upon which based its argument. Hydro One recast the information presented which showed that there is minimal variance in 2007 between the forecast load after CDM and the actual weather-normalized load are taken into account.

CCC noted that there is an information gap that needs to be filled for future load forecasting. It urged the Board to require Hydro One to come forward in its next rates case with a detailed proposal to incorporate the impacts of CDM into its load forecast. It also argued that there is a need for developing a detailed and comprehensive approach going forward for the sector, and to that effect referenced the Board's comments in the recent decision dealing with Toronto Hydro-Electric System Limited's ("Toronto Hydro")'s 2008 rates.

Board Findings

In the Board's view, the Company adequately explained in its reply argument that it has not used the 1,000 MW estimate assumed by VECC and that, in response to AMPCO's concerns, the 2007 historical variance between forecast load after CDM impacts and the actual weather-normalized load is minimal. The Board accepts Hydro One's load forecast as filed for purposes of setting 2008 rates.

With respect to CCC's comments, the Board endorses the comments made in the recent Toronto Hydro case.

"In a number of utility applications for rates in 2008, the specific effect of CDM activities on throughput has been impossible to quantify with any reasonable degree of accuracy. This means that an important area of public policy, supported by considerable funding through distribution delivery rates, as well as through direct OPA program funding under the global adjustment, is not measurable according to a consistent and well understood methodology. This lack of alignment between the OPA forecasts and those generated by individual utilities also has implications for LRAM and SSM [Shared Savings Mechanism] claims and calculations. LRAM and SSM claims are limited to the demonstrable effects of the specific utility's CDM programs on its throughput and revenue. In order to make this assessment, such effects must be empirically accounted for. The effects of CDM activities that are not attributable to the specific utility's actions must also be definitively accounted for."

Accordingly the Board finds that the effects of CDM activities not attributable to the Company's actions must be accounted for and requires Hydro One to come forward in its next rates case with a detailed proposal to incorporate the impacts of CDM into its load forecast, both those attributable to its own actions and those not attributable to the Company's actions.

3.

3. Conservation and Demand Management

Lost Revenue Adjustment Mechanism

In its April 12, 2006 decision dealing with Hydro One's rates (RP-2005-0520/EB-2007-0378), the Board directed Hydro One to produce a bottom up forecast of CDM impacts and also to propose a Lost Revenue Adjustment Mechanism ("LRAM") in its next rates case.

In response to the Board's directive, Hydro One's evidence in the current case was:

Hydro One has concerns with the practical difficulties and related accuracy of determining the actual amount of CDM savings achieved by its customers in a given year, through the implementation of CDM initiatives from various sources such as the Ontario Power Authority, Provincial Government and Federal Government. Hydro One believes it is prudent to wait for the OPA to develop Measurement and Verification programs for determining actual CDM achievements and as such is not proposing or requesting an LRAM at this time.

Instead, Hydro One's proposed rates reflect an assumption for CDM impact derived by taking the OPA's provincial CDM forecast and pro-rating it to Hydro One's service territory.

The Green Energy Coalition ("GEC") argued that since the OPA has indicated that it will continue to provide annual reports of province-wide CDM results, it would be appropriate for the Company to calibrate and eventually clear an LRAM using the assumptions reflected in its load forecast. In GEC's view, the status quo is unacceptable as it provides an incentive to a utility such as the Company, to fail at CDM while benefiting financially.

All other intervenors who commented on the subject supported the Company's approach for the reasons cited by the Company.

Board Findings

The CDM incorporated in Hydro One's load forecast is based on a top-down estimate of total CDM savings, not just those from CDM programs implemented by Hydro One. The OPA is just starting to establish the necessary Evaluation, Measurement and Verification processes. There is neither a detailed understanding of the expected savings from CDM programs that were incorporated in the load forecast used for rate setting purposes nor proper Evaluation, Measurement and Verification processes to establish the actual savings achieved through CDM programs. Furthermore, Hydro One does not have Evaluation, Measurement and Verification results for CDM programs initiated by entities other than the OPA. For these reasons, it is premature in the Board's view to put an LRAM in place for Hydro One at this time. In making this finding, the Board considered GEC's concern that the status quo will provide an incentive to Hydro One to fail at CDM. As stated earlier, the Board requires Hydro One to come forward in its next rates case with a detailed proposal to incorporate the impacts of CDM into its load forecast, both those attributable to its own actions and those attributable to other factors.

Operations, Maintenance and Administration

The Company seeks an increase in controllable Operations, Maintenance and Administration ("OM&A") spending amounting to \$45 million, an 11 percent increase over the 2006 approved level.

In considering any proposal for increases in spending the Board attempts to place the Company's current budget within historic norms. While sharp deviations may be justifiable on the basis that issues have arisen that require extraordinary attention, the Board considers that past spending is a useful guide in assessing spending proposals.

The parties expended considerable effort in their submissions in addressing the question as to what is the appropriate comparator for the Company's proposal.

Intervenors took the position that the appropriate comparator for the Company's proposal in this case was the 2006 actual spending levels. The Company on the other hand argued that 2007 spending was really the appropriate benchmark against which its current spending proposal should be measured.

It is to be noted that the Company's rates were last set as the result of a cost of service examination for 2006. Rates in 2007 were set using the Board's second-generation incentive rate mechanism. This means that the spending in 2007 was not subject to Board review for purposes of setting rates.

The Board agrees with intervenors that the appropriate comparator is 2006 actual spending in controllable OM&A spending. Applicants must always be mindful that spending decisions taken without Board oversight during bridge years may not be considered to be as supportable as expenditures undertaken after a Board review, such as a cost of service proceeding.

Having said that, in assessing any spending proposal the Board is also obligated to consider the basic justification and support offered by the Company for its specific spending programs. The simple fact that spending for this Company increased substantially in 2007 does not by any means, or in any degree, justify increases for the 2008 rate year.

By the same token, where the Company can show that its proposed expenditures in 2008 are justifiable in and of themselves, the fact that the overall spending exceeds historic norms is not fatal to the proposal.

Of the \$45 million increase sought by the Company, \$26 million is attributable to the enhancement of its vegetation management program. This is a result of the Company's proposal to increase the activity to reflect an eight-year cycle, rather than the current 10 to 11 year rotation.

The justification advanced by the Company for this innovation is rooted in enhanced reliability to its customers, many of whom live along relatively long stretches of exposed line. The Company presented evidence that showed that many other utilities have adopted a tighter rotation cycle for vegetation management, and that the tighter schedule offered marked improvement in the incidence of service interruptions associated with downed lines.

Some of the intervenors took the view that the fact that the Company appears to currently meet applicable reliability standards argues for a denial of the increased spending associated with it.

More pointedly, some intervenors have also suggested that the studies relied upon by the Company in support of its proposal show that the Company is not among the most efficient or effective utilities in conducting vegetation management. In particular the Board notes the extensive arguments advanced by AMPCO and VECC which suggest that the Company's efficiency in this area may be lagging somewhat for reasons independent of the vegetation management cycle it currently employs. That is to say that its inefficiency will not be resolved simply by adopting the eight-year cycle.

Board staff suggested that it may be more appropriate to accelerate the vegetation management program even more aggressively than is being proposed by the Company, to a six-year cycle. This suggestion is rooted in an observation that a six-year cycle may provide optimal vegetation management for a utility such as the Company.

Board Findings

The Board supports the Company's proposal with respect to vegetation management, but will impose some conditions to ensure that efficiencies are identified and acted upon by the Company.

The fact that the Company currently meets conventional reliability standards is not an end state, and the Company needs to be aggressive in seeking improvements in reliability. While the Board does not favour goldplating the system in pursuit of reliability standards that are well in advance of industry norms, that does not appear to be the case here. The conventional measures for reliability have never been accepted by the Board as definitive. Moving to an eight-year cycle is expected to result in improved reliability for the Company's customers.

The Board considers the increased spending associated with this program to be of a nature that brings it outside of a simple application of historic norms driving spending approvals. While the cost is somewhat high, this innovation appears to be justified.

The Board is concerned however that the Company does not appear to be pursuing efficiency in the delivery of these programs as aggressively as possible. The high level distribution benchmarking study undertaken by the PA consulting group (the "PA Study") suggests, but does not prove, that the Company's per unit costs for delivering this kind of program are higher, perhaps substantially higher, than other utilities.

The Board is also concerned that the cost structure of the Company, unless it is placed within reasonable boundaries based on appropriate comparisons, will simply continue to rise with successive labour agreements or supply contracts without effective restraint or improvements in efficiency.

It was suggested by some intervenors that the Board ought to reduce the Company's proposal to a level commensurate with other utilities reflected in the report. The Board does not accept this approach because the PA study is not sufficiently definitive with respect to the genuine comparability of the participating utilities and does not provide sufficient basis to order a reduction.

The Board is determined however, in this aspect of the case and in others, to attempt to create an evidentiary foundation for more fruitful comparisons in the future. The Company has been subject to a number of Board ordered studies generally directed towards creating a useful basis for comparison between its costs and the cost of comparable utilities. This has proved to be a somewhat elusive enterprise.

Accordingly, the Board will require the Company, in consultation with the intervenors and Board staff, to develop a benchmarking approach which will provide the Board at the next rebasing exercise with definitive information respecting the Company's relative efficiency in this area of operations. In the interim, the Board will expect the Company to give effect to any innovations which improve its productivity and efficiency in this area.

The balance of the increase in controllable Operation, Maintenance and Administration ("OM&A") spending amounts to \$19 million, an increase of approximately 4 1/2% as between 2006 and 2008. As the Company points out, this level of increase is less than the rate of inflation.

VECC suggested that disallowances should be ordered with respect to the cost of living adjustment component of the Inergi contract, the sharp increase in customer impact assessments associated with the Renewable Energy Standard Offer Program ("RESOP") program, and telecom services provided by its affiliate

The Board does not accept VECC's proposition with respect to the inappropriateness of the cost of living adjustment embedded in the Inergi contract. Such provisions are conventional within supply contracts of this kind, and any attempt to negotiate its removal would be likely to result in a costly set off, perhaps a disproportionate set off.

The Board requires regulated utilities to enter into commercial arrangements for the provision of services that are reflective of market conditions, and the Inergi contract appears to satisfy this requirement.

As to the RESOP program, the Board does not consider the absorption of these costs by the ratepayers to be unreasonable given the fact that the program originates with an agency of government, driven by a very explicit government policy favouring the consideration of renewable energy sources within distribution systems. It is true that this program has resulted in a very considerable and perhaps unanticipated volume of additional work associated with the vetting of these applications. It is not unreasonable for the ratepayer to bear the burden of this activity. It is to be hoped that as time goes by the demands of the program will abate, or the Company's ability to deal with it may improve. In the interim, the costs of coping with the volume of requests associated with the program are a reasonable system-wide burden.

The Board takes a different view with respect to the shared services activity provided by Hydro One's telecom affiliate. It is clear that the provision of these services by an affiliate is subject to the Board's rules respecting the costing of service contracts. It is apparent from the testimony of the Hydro One witness that the costs to the Company associated with these services have increased significantly as between 2006 and 2008. In 2006 the costs associated with this service arrangement were \$6.4 million. In 2008 they are expected to be \$9 million according to the updated evidence. Hydro One stated that these increases are attributable to increases in labour and pension costs experienced by its telecom affiliate, which had not previously been passed on to affiliates within the Hydro One group of companies.

Whatever the origin of these increased costs, it is incumbent on the Company to ensure that each of its affiliate service arrangements meet the requirements of the Affiliate Relations Code. This means that these assessments need to be current, especially when significant cost increases are being sought. In the circumstances the Company should have provided a current assessment of the extent to which the revised costs represent fair market value for the service. It is impossible at this stage to make an assessment for the purposes of this decision.

The Board finds that some disallowance is warranted given the failure of the Company to reassess the costs in light of the increases sought. Accordingly the Board will decrease the cost attributable to this activity by \$1 million, to \$8 million an amount which

exceeds the 2006 cost level, but falls short of the \$9 million sought. The Company is reminded that the obligation to ensure that affiliate services are being provided on a genuinely cost-effective basis is always a current obligation, and cannot rest on a one-time assessment.

Virtually every intervenor expressed some frustration with respect to the nature of the evidence supporting the company's compensation proposal. This area has been a challenge for the company, intervenors and the Board for some time. It appears as though the company is preparing a more informative benchmarking evidence for the purposes of its transmission application. As noted above with respect to the vegetation management issue, effective benchmarking is absolutely crucial for this Company and the ratepayers' interest going forward. Without such information, which takes into account the interests of both the ratepayers and the Company, it is difficult to judge the adequacy or inadequacy of the company's proposal. Accordingly, most parties deferred their concerns on this subject matter for consideration in the context of the transmission case where it is hoped a full and fruitful examination of the Company's relative compensation costs can be conducted.

Capital Expenditures and Rate Base

The Company proposes an increase in rate base equivalent to \$662M or 17.8. percent over the 2006 actual amount¹.

Concerns of the intervenors focused on the expenditures associated with the Cornerstone project, which is a comprehensive reconstruction of the Company's information technology capability. In fact, the intervenors' concerns lie not so much with the expenditures associated with the Cornerstone project which have been considered in previous cases and approved, but rather with the treatment of the savings associated with the implementation of the Cornerstone project in the coming years. Hydro One has forecast that the implementation of the Cornerstone project will result in approximately \$200 million worth of savings to the Company as a whole. About \$60 million of these savings are attributed to the distribution side of the business. It is integral to the Company's proposal that there be no recognition for 2008 rates, and accordingly no recognition within the third-generation Incentive Rate Mechanism ("IRM") period of these savings.

¹ ExD1/T1/S1 & Hydro One Reply Argument, pages 27/28

The intervenors take the view that the Board should impose a reduction in revenue requirement to reflect the anticipated savings associated with the project during the incentive regulation period. Otherwise, they contend, ratepayers will be denied the benefits associated with the Cornerstone project until rebasing, four years hence.

Board Findings

The Cornerstone project has been developed over a number of years and it is an accident of timing that the third-generation IRM will operate to insulate some of the savings associated with the project. As a result the Company will have a period where it alone enjoys the benefits of the efficiencies resulting from the Cornerstone project. This, however, is how incentive rate mechanisms operate. It would be inappropriate and contrary to regulatory principle for the Board to intervene a situation such as this to deny the Company this benefit prior to the next rebasing. The Board therefore will make no adjustments to the revenue requirement to account for future savings resulting from the Cornerstone project.

Regulatory Treatment of Smart Meters

Hydro One proposed recovery of smart meter costs for 2008 in its proposed rates. This proposal treats smart meters as if they were like any other distribution network asset. Hydro One forecast \$164.8 million in capital expenditures in the 2008 test year. Hydro One's evidence shows that \$136.5 million (83%) of the \$164.8 million smart meter capital spending forecast for 2008 relates to minimum functionality and the remaining \$28.3 million (17%) is for activities associated with "beyond minimum functionality" capabilities and features.

Board staff submitted that the Board has dealt with the matter of smart meter cost treatment in other 2008 cost of service decisions, and has adopted a consistent approach when dealing with such costs. The Board's approach has been to allow inclusion in rate base of capital costs for smart meters actually installed – in other words, historical costs. Ongoing costs (i.e., in the test or rate year) should continue to be tracked in the established deferral/variance accounts. In Board staff's view, no evidence was presented to suggest the Board should treat Hydro One's request in a manner inconsistent with recent Board decisions.

Board staff also noted that Hydro One's costs for smart meters include amounts for "beyond minimum functionality". The "beyond minimum functionality" capabilities are built into the smart meters and other equipment being deployed. These features are generally intended to improve service by allowing Hydro One to detect and more efficiently respond to outages. Although "active" once the smart meters are installed, these features are not currently "used and useful" as Hydro One has not upgraded its network management capabilities to operationally take advantage of these features.

Energy Probe, the Canadian Manufacturers and Exporters ("CME"), VECC, AMPCO and SEC submitted that Hydro One's smart meter costs should receive the same treatment as the Board decided in the Toronto Hydro 2008 distribution rates case. CCC also noted that this approach was also adopted in the Enersource Hydro Mississauga Inc. and Hydro Ottawa Limited 2008 distribution rate applications which were subject to settlement agreements accepted by the Board. Specifically, forecasted smart meter operating and capital costs for 2008 should continue to be tracked in the established deferral/variance accounts 1555 and 1556, and the existing smart meter rate adder should continue. Costs for meters installed to December 31, 2007 should be allowed in rate base, with the exception of costs for "beyond minimum functionality" features.

AMPCO did not oppose "beyond minimum functionality" costs related to super-capacitors in meters and associated equipment since these will benefit customers through improved outage response and service reliability, but submitted that features for Time of Use ("TOU") pricing should not be approved until these are implemented.

The Power Workers' Union ("PWU") supported Hydro One's proposed smart meter costs for both "meeting minimum functionality" and "beyond minimum functionality".

At the oral hearing, Counsel for Hydro One stated that the Company was aware of the Board's decision in Toronto Hydro's rate case and had no "good reason" to be treated differently.² In Argument-in-Chief, Hydro One maintained its preference that "all these costs be approved for recovery as a regulatory asset up to April 30th, 2008 and be included in its core work program beyond that time for recovery as part of its revenue requirement."³ However, in light of the Toronto Hydro decision, Counsel for Hydro One

² Transcript, Vol. 2, p. 70 ll. 10-26

³ Transcript, Vol. 7, p. 24, l. 28 to p. 25, l. 3

also presented the Board with an alternative scenario whereby all smart meter costs up to December 31, 2007 be approved for inclusion in rate base. Costs beyond December 31, 2007 would continue to be tracked in deferral accounts and the smart meter rate adder would continue at the current Board approved level.⁴

Hydro One, in its Reply Argument, amended its proposal as follows:

On reflection, a faithful application of the principle established in THESL [Toronto Hydro] would see these costs approved to the time of review. In the case of THESL that was December 2007. For Hydro One it would be mid-year 2008. This approach has the added advantage of maximizing the total credit balance to be returned to ratepayers when consideration is given to all regulatory assets. Therefore, for consistency of regulatory asset treatment, the Company proposes that smart meter costs be cleared as of April 30, 2008, along with all other regulatory assets, particularly given the mitigation benefits to customers of clearing all regulatory accounts as of that date.⁵

Hydro One submitted that smart meter expenditures from January 1, 2008 would continue to be tracked in the established deferral accounts and the interim rate adder would continue.

Board Findings

In mid-2007 the Board conducted a combined smart meter proceeding under file EB-2007-0063 to review actual smart meter costs for installed smart meters for the thirteen distributors then authorized by regulation to undertake smart meter activities. In its Decision with Reasons, the Board concluded:

Restricting cost recovery to installed meters is consistent with the Board's Decision on the methodology to recover costs in rates. This Decision allows the utilities to incorporate the capital costs for installed smart meters in rate base, and to calculate the revenue requirement on that basis. It is true as pointed out by some that even installed meters are not necessarily operational in the sense that they are not integrated with the network and that utilities are not calculating bills on the basis of time-of-use pricing. However, they are installed as opposed to sitting in inventory,

⁴ Transcript, Vol. 7, p. 42 l. 24 to p. 42 l. 13

⁵ Hydro One's Reply Argument, p. 33.

and they are being used to calculate bills. In the circumstances, the Board believes this to be an appropriate approach.⁶

The Board has adhered to this approach in subsequent decisions for 2008 distribution rate applications. Specifically, in the Board's Decision with Reasons on Toronto Hydro's application for distribution rates for 2008-10, the Board accepted the inclusion of actual costs for the historical period, but concluded:

While the Board has accepted the Company's capital expenditure forecasts related to smart meters for 2008 and 2009, the Board shares the concerns expressed by parties with respect to the Company's proposed regulatory treatment.

... While the Board accepts that the Company is now in a better position to forecast its costs associated with smart meters, the Board is of the view that there is still considerable risk that the Company's forecasts may be substantially off the mark, resulting in significant over- or under-recovery. The issue is not necessarily that smart meter installation expenditures may not materialize; rather, the concern is the potential of timing differences in the actual expenditures from those forecasts. Timing differences will always exist, however, neither the Utility nor ratepayers should benefit or be burdened by an initiative that is temporal in nature and can be reasonably viewed as a cost pass-through. Treating smart meter expenditures for rate making purposes like any other core distribution activity is premature. The Board sees no harm in permitting the current regime to continue as it offers protection for both the Company and ratepayers from the vagaries of missed forecasts. As the installation program progresses and once the Board has reviewed and approved actual expenditures, bringing these expenditures into rate base can be considered again.

The Board therefore does not accept the Company's proposal to include the forecast capital expenditures in rate base for the 2008 and 2009 test years. The current regime where these expenditures are funded through a smart meter adder shall continue, as shall the variance accounts mechanisms currently in place to enable true-ups.⁷

Approving only actual and audited costs is also consistent with the Board's general policy with respect to requests for disposition of deferral and variance account balances. The Board interprets that Hydro One's amendment in its Reply Argument as dealing

⁶ Decision with Reasons EB-2007-0063, August 8, 2007, pp. 14-15.

⁷ Decision with Reasons EB-2007-0680, May 15, 2008, p. 24.

with the balances of the deferral accounts for disposition, rather than adjusting the date for the installed smart meters and associated capital costs be revised.

Those parties that have examined and made submissions on this matter have overwhelmingly submitted that Hydro One's smart meter costs should receive the same treatment as the Board decided in the Toronto Hydro case. While Hydro One's preference is for approval of the 2008 test costs in rate base and revenue requirement, Hydro One, both on the stand and in Argument-in-Chief and Reply Argument, acknowledged that that it could not provide reasons that it should be treated differently.

The industry and the Board have developed a body of policy and precedent related to smart meter costs in a number of cases over the last few years. The Board's treatment has evolved. Further, the Board views its approach as facilitating smart meter deployment as distributors become authorized, managing rate impacts in the long-run and ensuring that costs with this new and evolving technology are incurred in a disciplined and prudent manner.

The Board sees no reason to deviate from its past practice, as established in the combined smart meter proceeding and the Toronto Hydro proceeding. Continuation of the smart meter rate adder and the deferral/variance accounting for costs past December 31, 2007 will still enable Hydro One to deploy smart meters in accordance with government regulations and objectives.

The Board approves Hydro One costs that meet "minimum functionality" for smart meters installed to December 31, 2007 in rate base. Approval is extended to the costs paid to Capgemini for smart meter project management in 2006-7. VECC argues that approval of these costs should be deferred but the Board is satisfied, on the evidence adduced, that that Hydro One has reasonably substantiated these costs. Costs for "beyond minimum functionality" capabilities in 2006-7 are also approved in rate base but the tracking of these costs should also continue, as the Board found in the case of Toronto Hydro.

Hydro One is directed to remove 2008 operating costs of \$9.7 million and capital costs of \$164.8 million. 2008 costs should continue to be tracked appropriately in the established deferral/variance accounts. Further instruction on the disposition of the deferral account balances for "minimum functionality" costs incurred for smart meters installed to December 31, 2007 is discussed under "Deferral and Variance Accounts".

Hydro One should, in its draft Rate Order, continue to use its current Board-approved smart meter rate adder of \$0.93/month per metered customer and track revenues received for the rate adder in the applicable sub-account of account 1555.

In accordance with Guideline G-2008-0002: Smart Meter Funding and Cost Recovery, the Board advises Hydro One that it may file for approval and recovery of actual and audited costs for smart meters installed in 2008 in a subsequent application.

Rate Design and Cost Allocation

This chapter of the Decision addresses Hydro One's proposed customer rate classes; cost allocation; revenue to cost ratios; and rate harmonization plan. This chapter also deals with specific relief requested by Rogers Cable, Milton Hydro and Hopper Foundry.

Hydro One's cost allocation and rate design proposals can be summarized as follows:

1. Reduce the 280 existing customer classes to 12 new customer classes;
2. Apply the Board approved cost allocation methods to allocate costs to the new rate classes subject to certain exceptions;
3. Establish rate levels and revenue-to-cost ratios for each customer class that are compatible with the Board's revenue-to-cost ratio guidelines;
4. Rebalance rates over four years so that the bill impact on an average customer within each class is no more than 10% per year; and
5. Terminate the Interim Time of Use Program approved by the Board by Order dated November 24, 2004.

The New Customer Rate Classes

Hydro One serves two categories of customers, Retail customers and Sub-Transmission customers.

Retail customers consist of Legacy customers (customers of the former Ontario Hydro) and "Acquired" customers (customers of some 88 distributors acquired by Hydro One, except for Brampton Hydro). Each of the Acquired Distributors had a number of customer classes at the time of acquisition, such as Residential, General Service < 50

kW, etc. Uniform rates were instituted in 2006 for certain classes such as Streetlighting (RP-2005-0020/EB-2005-0378). However, for most Retail customers the rates of the Legacy system and the Acquired distributors are still distinguished from each other in Hydro One's current tariff (EB-2007-0626). In Hydro One's Application, the Residential customers of the Acquired Distributors, which account for some 14% to 15% of the total customer base of Hydro One, will be combined with the Residential customers of the Legacy system, and General Service customers will be combined with classes with similar Legacy customers.

Hydro One is proposing a single class of customers to be called the Sub-Transmission class ("ST Class") for embedded distributor supply points regardless of voltage, and all three phase customers with demands above 500 kW connected at 13.8 kV or above. These customers are currently in a variety of Legacy and Acquired classes. This issue is considered in the section dealing with Sub-Transmission class.

As indicated, Hydro One proposes to reduce the current 280 rate classes to 12. Those 12 proposed classes are described in the table below.

Abbreviation	Class of customer
UR	Urban Residential (High Density)
R1	Residential (Medium Density)
R2	Residential (Low Density)
Seasonal	
UGe	Urban General Service Energy Billed
UGd	Urban General Service Demand Billed
GSe	General Service Energy Billed
GSd	General Service Demand Billed
Streetlighting	
Sential Lights	
ST	Sub-Transmission
DG	Distributed Generator

The object is to simplify the rate class structure in a manner that better reflects the utilization of assets and cost causality. Originally, Hydro One proposed 10 rate classes but modified its proposal based upon submissions from stakeholders. Of the 12 new rate classes proposed, four are designed for residential customers. The number of customers in each of the residential classes is set out in the table below.

Residential Classes

2008 New Rate Class	# of Customers
Urban Residential High Density	155,840
R1 Residential Medium Density	365,190
R2 Residential Low Density	358,328
Seasonal Residential	154,437
Total	1,033,795

(Ex. G1, T2, S3, pp. 2-4)

Hydro One proposes to allocate customers to the different classes based on Hydro One’s existing density criteria. A number of the intervenors questioned the use of the density criteria particularly for urban classifications. Hydro One defines the urban classification criteria as 60 customers per km and a minimum critical mass of 3,000 contiguous customers. AMPCO notes that while this criteria has been used for a number of years no rationale was offered for its use.

The Urban Residential class pays a significantly lower fixed charge than the R1 class and a slightly lower volumetric charge. AMPCO suggests that applying the proposed density and critical mass criteria causes most of the residential customers in the Acquired Distributors group to be classified R1 and not UR. As a result, this split may produce much of the cost increase for the ratepayers of the Acquired Distributors.

Hydro One also proposes to reclassify the current Unmetered Scattered Loads (“USL”) class to the General Service energy billed class. There would however be a credit for USL customers within the class because they have no meter costs. This issue is discussed in greater detail in the section dealing with Unmetered Scattered Load.

CME and SEC submitted that combining the customers of Acquired Distributors and the Legacy class in one class does not recognize that the rates for the customers of most Acquired Distributors were lower than the rates for the Legacy customers. SEC submitted that a separate cost of service analysis for the Acquired Distributors is required. This, they argue, is necessary if uniform rates are to be charged for the combined classes.

CCC supported Hydro One's proposed rate class structure and commended Hydro One for accommodating the requests of stakeholders in developing this proposal.

Board Findings

The Board finds that the definitions of the proposed classes and the criteria for reclassification of customers are reasonable. These are long standing criteria accepted by the Board since 1996 and it is not apparent to the Board that a more appropriate alternative is available.

There are always boundary issues when classifying customers. Based on the evidence, the Board accepts Hydro One's judgement with respect to the proposed classes for the purpose of this decision. Moving from 280 rate classes to 12 new rate classes is not a simple exercise.

A number of the intervenors questioned the density criteria used to determine the residential classes. The Board recognizes that combining the customers of the Acquired Distributors with customers of the Legacy distributors is controversial. There may, as SEC argues, be significant cost differentials. Notwithstanding that concern, the process needs to move forward. In the circumstances, the Hydro One proposal is a reasonable initial step. As indicated in section 7.4 of this decision the Board will require further studies to improve the understanding of the allocation.

Accordingly, the Board will require Hydro One to re-examine the practicality of additional class definitions to improve understanding of cost causality. This should be done in the context of additional cost allocation research, and the matter is discussed in more detail in section dealing with the Proposed Cost Allocation.

Sub Transmission Class

The Sub Transmission Class ("ST Class") is distinguished from the other classes in the cost allocation study because costs are not allocated to primary and secondary lines but only to sub-transmission lines.

The Intervenors with the exception of the ECMI support the ST Class proposed by Hydro One.

VECC supported the creation of the single ST Class including both embedded distributors and large retail customers noting that these customers generally utilize the same assets. One concern advanced by VECC was that some of the embedded distributors are served at voltages below 13.8 kv, the dividing point for the ST Class. VECC noted that from a service voltage and facility use perspective these delivery points are similar to large General Service customers. However, VECC acknowledged the need for a standard approach for all embedded distributors and supported the classification of these customers as ST Class customers.

ECMI argued that all embedded distributors should be grouped in a separate class and not in the ST Class. Hydro One responded that contrary to ECMI's assertion that all delivery points to LDC's have stable loads and are homogeneous, that is not the case. For example, one LDC delivery point has a load factor of 9% illustrating the fact that not all LDC delivery points have similar patterns of consumption. As indicated in Exhibit H1.132 the largest ST customer is an embedded distributor with a demand of 265 megawatts and the smallest ST customer is also a distributor with a demand of 100 kilowatts. Hydro One argued that this illustrates that LDCs are not necessarily similar to each other, and that a separate customer class comprising them would not be sufficiently homogeneous.

ECMI argued that business risk should be one of the required customer classification criteria. Hydro One responded that there is no precedent in this or past proceedings supporting the use of this criteria. Nor did ECMI explore this concept with any witnesses during the proceeding. The Distribution Rate Handbook released by the Ontario Energy Board ("OEB") in 2001 defines customer classes to be used for distribution rates. There is no indication that customer classes should be determined based on business risk.

Board Findings

The Board rejects the ECMI proposal that customer classes should be based on the degree of risk. As Hydro One pointed out, this would be a novel concept. There is virtually no evidence in this record that would allow the Board to seriously consider this proposal.

Unmetered Scattered load

Rogers Cable (“Rogers”) intervened in this proceeding to oppose Hydro One’s proposed treatment of Unmetered Scattered Load (“USL”) accounts, which are load using devices that do not have individual meters. Hydro One proposes to reclassify the current USL class to the General Service energy (“GSe”) billed class. There would however be a credit for USL customers within the class because they have no meter costs.

There was some discussion as to whether USL should be a separate rate class.

Hydro One proposed a USL meter credit to recognize that the utility avoids the costs associated with meter management when providing service to this customer class. AMPCO and VECC supported this treatment. CME did not take a position. There was discussion as to the amount of credit this class should receive and why, which is reviewed below. In the end, the issue really centred on the amount of the credit to be extended to this class of customers.

Rogers does not question that Hydro One has properly derived the credit amount with respect to reduced metering costs. However, Rogers argued that this credit does not reflect other cost differences. They argued that because the class has a relatively flat load profile, USL customers cause less costs than General Service customers, whose loads fluctuate considerably over the course of the day and season. Rogers also noted that Hydro One did not provide a revenue-to-cost analysis for the proposed 2008 USL rates.

Further, Rogers claimed that Hydro One has inappropriately classified all USL customers with the non-urban GS class even though 392 USL connections are located in urban areas that qualify for lower urban general service rates. Rogers noted that the energy charge for rural general service energy billed customers is more than 160% of that for urban general service energy billed customers.

Rogers claimed that the impact of recovering the relatively small revenue decrease that would result from reclassification of these 392 USL would be minimal.

Rogers submitted that the Board should direct Hydro One to apply a fixed charge credit to non-urban USL rates in order to bring the USL revenue-to-cost ratio within the range provided for in the Board’s Report on Cost Allocation. This, Rogers said, would yield a

USL credit of \$20.65 for non-urban GSE class as opposed to the \$6.86 proposed by Hydro One.

Rogers also asked the Board to order Hydro One to reclassify the 392 USL connections that are physically located in urban density areas to the UGe class and to apply UGe rates net of the Hydro One derived metering credit of \$6.65.

AMPCO supported Hydro One's inclusion of USLs in the GSe class, with a metering credit. AMPCO opposed the treatment advocated by Rogers, noting that special consideration for any group would require both revisiting the cost allocation process and possible establishment of a separate class for a particular type of unmetered equipment. AMPCO noted that a detailed review may well result in a higher cost allocation than Hydro One currently proposes or a requirement that higher energy use equipment be metered.

VECC noted that providing a credit to USL customers recognizes the material cost differences between servicing USL loads versus other small general service loads. VECC noted that the load factor for USL loads is in the range of that for other customers also included in the GS energy billed class. As a result, VECC concluded that there was no compelling reason to create a separate USL class at this time.

Board Findings

Rogers argued that ideally the USL connections should be identified as a separate class of customers and USL rates be set on a proper cost allocation study for such a class. Rogers noted this is currently done for two specific types of USL connections, street lighting and sentinel lighting.

Rogers did not question the amount of credit proposed by Hydro One for the USL class to reflect the lack of metering costs. Nor was this credit opposed by the other intervenors.

The dispute turns on other credits that Rogers is seeking and in particular an additional credit for USL connections that are physically located in urban areas and a credit for those connections that have a flat load.

Rogers attempted to estimate the amount of these credits in its argument. As Rogers concedes, the data is limited. The Board does not have proper information in this record to calculate potential cost reductions relating to these additional matters. The Board is convinced that the best way to approach these additional issues is through the rate design process currently under way in the Board's initiative on Rate Design [EB-2007-0031]. This review will consider the need for changes to distribution rate design in light of industry changes and emerging issues. In the circumstances of this case, the Board accepts the USL rates and the USL credit proposed by Hydro One.

The proposed Cost Allocation

After developing the appropriate rate class structure, Hydro One allocated costs to these rate classes. In Hydro One's 2006 rate case⁸ the Board rejected the utilities harmonization proposal because it was not supported by a cost allocation study. In the current application, Hydro One relied on the Board's cost allocation methodology detailed in the EB-2005-0317 Report of the Board⁹ with modifications to take into account new rate classes proposed by Hydro One.

CCC submitted that Hydro One had met the Board's directives in conducting the cost allocation study based upon the new rate classes for 2008. CME also agreed that the Board approved cost allocation methods should be applied to allocate Hydro One's cost of service to the new rate classes. CME noted that, with few exceptions, Hydro One had applied these cost allocation methods correctly. The exceptions related to the provision of Sub-transmission service to embedded customers, the application of density weights to reflect the primarily rural nature of Hydro One's system and the large number of customer classes.

The customer classes in the cost allocation study are the twelve classes proposed by Hydro One. Most of these classes include customers of the Legacy and Acquired Distributors.

SEC submitted that a separate cost allocation study should have been conducted for the Acquired Distributors because the lower rates may indicate lower costs. Hydro One

⁸ RP-2005-0020 / Eb-2005-0378

⁹ Cost Allocation Review: Board Directions on Cost Allocation Methodology for Electricity Distributors, September 29, 2006

responded that a separate study cannot be performed because costs are not recorded separately by Hydro One for the Acquired and Legacy systems.

The customers in the Acquired Distributors areas generally have lower rates than those in the legacy areas. Combining the customers in the Acquired Distributors with the Legacy customers means that the customers in the Acquired Distributors will have a substantially greater rate increase. SEC in particular, questions the legitimacy of this exercise and the assumptions that Hydro One is using.

Hydro One essentially argued that low rates likely reflected the fact that revenues were not covering costs in those areas. Accordingly, they assumed that Legacy customers were subsidizing the Acquired customers. SEC and others noted that there was no separate analysis of costs in the Acquired Distributors territories and it was unreasonable to assume that revenues were not covering costs simply because prices were lower in these areas.

Hydro One's cost allocation incorporates the concept of density weighting for overhead lines and for transformers. For example, lines have differing lengths and differing numbers of customers per km, and total feeder length is allocated proportionately to the rate classes, based on the number of customers of each class on each feeder. Hydro One submitted that the density weights are determined by the average distance between customers in the respective classes. Hydro One also considers factors related to energy and the net book value of assets used to provide service to the classes.

VECC submitted that the concept of density weights should have been developed more fully and applied to the split of Sub-transmission lines and transformation costs between the ST Class and other classes. Hydro One responded that density weights are applicable only where there is a distinction between urban and rural customers that would otherwise be in the same class.

CME also stated that Hydro One should have determined the costs and revenues allocated to Acquired Distributors on a stand alone basis. Hydro One responded that this exercise is impossible because Hydro One does not track costs separately for each Acquired Distributor. Hydro One also noted that where utilities merge, the Board requires a cost allocation study for the consolidated entity.

SEC also questioned the density factors that Hydro One used to allocate costs amongst the urban and normal-density classes, and submitted that Hydro One had not provided adequate evidence to show that the allocations affected by density factors are appropriate. SEC submitted that not all costs affected by density are captured by the factors. Vegetation management, they suggest, is an example. In its argument SEC suggested that benchmarking would be an appropriate method to analyze costs within Hydro One's service territory.

Hydro One replied that the density weights are based on energy and distance for distribution lines, and net book value and energy, in addition to the distance factors. The density factors are a proxy to reflect the cost difference between rural locations and towns. Hydro One does not accept the criticisms of their use of density factors. They argued that the study proposed by SEC is not possible because costs are not recorded separately for the Acquired Distributors and for the Legacy system.

VECC suggested that density weights should have been applied to the split of Low Voltage ("LV") assets and Primary assets between the ST and other classes. VECC noted that the ST, DG, Street Light and Sentinel Light classes should also have been considered when developing the density weights. Hydro One disagreed, replying that DG, ST, Street Light and Sentinel Lights are not classes that are divided using density between Urban and Rural, like Residential and General Service.

Board Findings

The Board accepts Hydro One's position that the difference between the current rates of Legacy and Acquired Distributor customers is not solely attributable to underlying cost differences.

The Board accepts that the rates in the Acquired Distributor service areas must increase by more than those for similar customers in the Legacy system. The Board remains concerned that there may be factors that make it less costly to serve the Acquired Distributor territories than Legacy systems but this conclusion cannot be reached on the basis of the cost allocation information provided by Hydro One. The Board agrees with the intervenors that Hydro One has not established that there are no significant differences in serving residential customers of Acquired Distributors compared to the Legacy customers.

Accordingly, the Board directs Hydro One to provide a more detailed analysis on the relationship between density and cost allocation to the Board. This should consider whether the number of Residential and General Service customer classes in the new class structure is adequate, and whether the customer class demarcations approved in this Decision offer the best reflection of cost causation. The study should include consideration of alternative density weightings, with descriptions and criteria for comparing alternatives. Comparisons with the costs of distributors similar in size and location to Acquired Distributors would also be useful. The Board requires that Hydro One submit this information in its next cost of service application.

It would have assisted the Board if Hydro One had been able to provide a cost study relating to the customers in the territories of the Acquired Distributors. Hydro One's response to this issue is that it does not have the necessary data because it only has "one set of books". The Board must accept that as a fact. However, as is indicated above, the Board expects Hydro One to provide comparative analysis to allow the Board to better assess cost differences between the Legacy and Acquired customers.

The Proposed Revenue to Cost Ratios

Hydro One relied on the revenue cost ranges contained in the Board's EB-2007-0667 Report ¹⁰ to develop its target rates for the new rate classes.

For those customer classes currently below the Board's recommended ratio, the rates were adjusted upward to achieve the minimum ratio. For those customer classes initially above the Board-recommended ratio, rates were adjusted down to the maximum of the range. As a result, Hydro One's proposed rates achieved the target revenue to cost ratios within the Board's approved ranges for each of the customer classes starting in 2008.

Hydro One's revenue to cost ratios are presented in two different ways. Both use the proposed customer classification. In the first case, the revenue from each class is proportional to the revenue of current approved rates. That is, the current rates are adjusted by a common factor to yield a total revenue requirement of \$1,067 million. These ratios represent the status quo.¹¹

¹⁰ Application of Cost Allocation for Electricity Distributors, November 28, 2007

¹¹ Exhibit G1/T3 /S1/Table 2

In the second case the class revenues are based on the proposed target rates. The revenue to cost ratios represent the long term objective that would result when all rates have been harmonized in each class across the entire service territory.¹²

The table below shows the status quo as well as the proposed revenue to cost ratios. Column 3 shows the applicable target range is based upon the Board's report Application of Cost Allocation for Electricity Distributors, EB-2007-0667, November 28, 2007.

Revenue to Cost Ratios			
Class	Status Quo Ratios Column 1	Proposed Ratios Column 2	Target Range Column 3
UR – Urban Residential (High Density)	0.87	1.0	0.85 – .15
R1 – Residential Medium Density)	0.82	0.88	0.85 – .15
R2 – Residential (Low Density)	1.04	1.04	0.85 – .15
Seasonal	0.92	1.0	
UGSe – Urban General Service Energy Billed	1.29	1.2	0.8 – 1.2
UGSd – Urban General Service Demand Billed	0.95	1.0	0.8 – 1.8
GSe – General Service Energy Billed	1.08	1.08	0.8 – 1.2
GSd – General Service Demand Billed	1.02	1.02	0.8 – 1.8
ST – Sub-Transmission	2.35	1.15	0.85 – .15
DG – Distributed Generator	1.63	1.0	
Streetlights	0.60	0.7	0.7 – 1.2
Sentinel Lights	0.62	0.7	0.7 – 1.2

¹² Exhibit G1/T3 /S1/Table 2

The proposed ratios are in the Board's target ranges, or at the nearest boundary of the range. Where the Board Report does not have an applicable range, for Distributed Generation and for Seasonal, the proposed ratio is 1.0.

CCC supported Hydro One's proposed target rates and the implicit revenue to cost ratios given that this is the first year that Hydro One applied the Board's cost allocation methodology. CCC agrees that it would be premature in absence of historical results to adjust all rates to achieve revenue cost ratios of 1.0. CCC supports the use of revenue cost ratios as a rate making tool but warns that a ratio of 1.0 for every rate class is not necessarily the objective because cost allocation and rate design are not precise mathematical exercises.

VECC submitted that the Board's policy range for Large Use customers does not apply to the ST Class, because the ST Class includes embedded distributors together with a variety of smaller customers. VECC noted that the Large User classes considered by the Board in other distributor's applications do not include such customers. VECC suggested that a ratio of 1.25 would be a suitable target. Hydro One pointed out that the ST Class includes the former Direct customers and argued that it is reasonable to adopt the same ratio that is used for the Large User class in other distributors.

AMPCO suggested that Hydro One should have a revenue to cost ratio closer to 1.0 and not move only to the policy range boundary. However, AMPCO did support the proposed ratio of 1.15 for the ST Class, as long as there is a commitment to move the ratio to 1.0 in the near future.

AMPCO did not support the proposed ratio of 1.0 for the Distributed Generation ("DG") class, arguing that there was not enough reliable data. They submitted that it is incongruous to have a ratio of 1.0 for a class with little historical information while having a ratio other than 1.0 where more accurate information is available. Hydro One replied that there was adequate data to support the DG cost allocation results.

VECC also opposed Hydro One's proposal to reduce the revenue cost ratio for the DG Class to 1.0. While Hydro One argued that this step supports government policy regarding DG. VECC did not accept this argument. VECC claimed that, considering the type of customers within the DG Class it should have an upper bound of 1.25.

AMPCO asked the Board to direct Hydro One to develop a clear plan to bring all of its customer rates into a narrow and consistent band of revenue to cost ratios of .95 to 1.05 over the harmonization period and to undertake the studies necessary to ensure that the cost allocation is accurate. AMPCO also stated that the Board should extend the harmonization period if necessary to meet this objective.

Board Findings

The Board notes that the proposed ratios apply to the end-state rates, and that the status quo ratios of the R1 and UGe classes are outside of the Board's policy range. In the case of UGe, the proposed ratio is at the boundary of the range, and the realized ratio will be outside the range until the final step of the harmonization process. In the case of R1, the realized ratio would presumably be within the range prior to the time of the next re-basing.

CME reiterated the submissions it made in the motion brought by AMPCO to review the Board's March 19, 2008 Decision regarding Oshawa PUC¹³. AMPCO's argument, which was supported by CME, was that the upper limits of the ranges should not be the ultimate rate design target. Rather, the ultimate revenue to cost ratio target should be unity. The Board's Report recognizes that inadequate revenue-to-cost data exists at this time to justify a rigid requirement to achieve unity. The Board notes that there has been movement to within the boundary range. That is all the Board requires at this stage.

The Board disagrees with the VECC and AMPCO position that the revenue cost ratio for the DG Class should not be one. As has been noted elsewhere in this decision, the Board's Cost Allocation Report found there was insufficient data to support unity as a definitive goal. However, the Board finds that with respect to the DG Class using a ratio of 1.0 is appropriate.

The Fixed/Variable Split for Each Rate Class

Hydro One has established fixed charges for each class to reflect those fixed costs such as billing, metering and allocated cost. AMPCO supported the fixed/variable splits for each class noting that Hydro One has not attempted to inflate fixed charges in order to

¹³ EB-2008-0099

reduce its exposure to fluctuating customer demand. AMPCO also noted that the proposed structure does not mute the price signal for customers seeking to save through conservation.

AMPCO also supported Hydro One's proposal to have both fixed and variable service charges within the proposed new ST Class. Under Hydro One's proposal, ST Class customers will pay a minimum fixed service charge of \$188.00 a month for each delivery point, which is a new charge for most customers in this class.

AMPCO, VECC and CCC submitted that Hydro One's proposed structure regarding fixed/variable splits is appropriate.

Board Findings

There is general support for Hydro One's proposal among the parties that commented on this issue. The intervenors noted that the Board has initiated a rate design consultative process to review the purpose and structure of fixed and variable rates. To the extent that generic recommendations are forthcoming, future changes to Hydro One's rate structure may be warranted. On this basis, the Board accepts Hydro One's proposal with respect to the fixed/variable split for each of the new rate classes.

Hopper Foundry

Hopper Foundry ("Hopper") intervened in this proceeding claiming that the rate increases proposed by Hydro One would result in a 300% increase in its electricity bill.

The company operates a foundry in Forest, Ontario. In 1991 when the company was served by the Forest Public Utility Commission ("Forest PUC") Hopper installed time-of-use meters and arranged to operate the foundry during off-peak hours. Forest PUC promoted this arrangement because the town grid could not support both the town and the foundry at the same time. Accordingly, Hopper was offered a special off-peak rate with a significantly reduced charge per kilowatt hour and no demand charge during off-peak hours.

Hydro One acquired Forest PUC in early 2002 and continued with the special pricing arrangement until the beginning of market opening in May 2002. Off-peak pricing was renewed by Hydro One in November 2004 when interim time-of-use rates were

introduced pursuant to a CDM plan approved by the Board¹⁴. At that time the extension of the program was characterized as a “pilot” project limited by the funding provided through the Board’s so-called Third Tranche CDM program. Hydro One now proposes to discontinue the time-of-use pricing because funding for the CDM Plan has expired. This results in the 2007 increase Hopper complains about.

One option offered by Hydro One was that Hopper upgrade its power system to receive electricity at a voltage consistent with the voltage proposed for transmission (“ST”) customer class. In final argument, Hopper estimated the cost at \$151,594.00 and requested that all costs be covered by Hydro One including the lost production costs while its power system is upgraded. Hydro One responded that if this solution was adopted by the Board, Hydro One should be able to recover these costs in its revenue requirement.

Hopper would prefer that the Board grandfather the current incentive rate structure. This, Hopper said, would not require any capital expenditure by either Hopper or Hydro One as “the only capital equipment needed to accomplish this is a pen”. Hopper further stated that acceptance of the current rates on a grandfathered basis confirms the wisdom of original pricing adopted by Forest PUC and accepted by Hydro One.

Hopper also noted that Hydro One has a million dollars in its budget for 2008 for continuation of Third Tranche Program CDM programs that had not been completed. These funds, Hopper argues, could be used, in part, to extend the current interim rate structure associated with the pilot program.

A number of parties supported Hopper including CME and AMPCO. Both note that it seems strange to discontinue interim rates at a time when the Province is investing millions in smart meters with a view to maximizing off-peak usage. CME notes:

“Hopper Foundry has been an existing customer of Hydro One and its predecessors for many years. It operates in the evenings. Hydro One’s distribution utilities providing service to the community in which Hopper Foundry is located are inadequate to enable Hydro One to satisfy the peak period demands of the Hopper Foundry 24 hours a day. Stated another way, Hydro One can only satisfy its obligation to serve Hopper Foundry by meeting its peak demand in the off peak evening period.”¹⁵

¹⁴ RP-2004-0203/EB-2004-0457 & RP-2004-0203/EB-2004-0461

¹⁵ CME Argument, para. 110

CME stated that until Hydro One has upgraded its distribution system serving Forest to the point where it can meet the peak demands of Hopper 24 hours a day, the off-peak interim utility program should remain available to Hopper.

Board Findings

None of the parties, including Hydro One, question of the legitimacy of the Hopper Foundry concerns. No one suggested that a rate increase of 300% per year can be tolerated without a serious mitigation initiative.

One of the options explored was to upgrade the Hopper system allowing Hopper to qualify for a new rate class and a lower rate. However, this involves a capital cost in excess of \$150,000.

That leaves the question of who should cover those costs. Hopper argued that it is not in a position to cover those costs. Hydro One stated that if it has to cover those costs it should be able to pass on these costs in its revenue requirement.

In the circumstances, the Board believes that the reasonable approach is to continue the existing time-of-use rates for the rate year terminating on April 30, 2010. While the Third CDM Program has technically been terminated, Hydro One did testify that they have a million dollars in the budget in 2008 to continue programs not completed.

The additional time will allow both Hopper to explore its options and take the necessary steps required to become a customer served under one of the approved rate classifications.

Milton Hydro

Milton Hydro objected to the rates that Milton is paying Hydro One for the M1 and M3 feeders from Hydro One Networks' Palermo transmission station to the Milton Municipal boundary. Milton currently pays \$0.633/kW for these feeders, which is the currently approved rate for "Shared LV Lines". Milton asked the Board to create a new category of line for the purpose of LV rate design called a "dedicated line". Under this definition, the M1 and M3 feeders, some 0.24 kms in length from Hydro One's Palermo station to the Milton municipal boundary would become dedicated lines.

Milton provided a definition of a “dedicated line” as “a line constructed to serve, and continues to serve, a single LDC’s load and aside from crossing a Networks transformer station property does not cross the area of any other LDC.” This differs from Hydro One’s definition of a “Specific line”, which is that it is owned by Hydro One, supplies solely one LDC and is within that supplied LDC. Hydro One further stated that the fact a line is dedicated does not make it “Specific” for rates purposes.

Milton stated that it paid Hydro One over \$500,000 from May 1, 2002 to January 1, 2008. If the two lines of 0.24 kms in length had been defined using Milton’s definition of a dedicated line, the payments over that period would have been just \$17,000. Milton adds that it has been paying nearly \$100,000 a year for five poles and two lines of 0.24 kms of wire with a book value of \$10,000 and a replacement cost of \$30,000.

Milton also complained that rules with respect to these lines are not being uniformly applied by Hydro One. They noted that two of the feeders that serve Oakville from the Palermo transmission station were actually built and owned by Oakville so Oakville does not incur the costs of the type that Milton is incurring. Milton says that if they owned the M1 and M3 feeders then there should be no charges whatsoever.

Milton first brought this matter to the attention of the Board in a letter dated April 24, 2007 to the Board’s Chief Compliance Officer who replied on July 26, 2007 that “he could not conclude that Hydro One is charging Milton LV Charges in a non-compliant manner”. Milton states that they continue to pay these charges under protest.

Milton has asked the Board to direct Hydro One to refund or credit Milton Hydro the difference between the amount they have paid from May 1, 2007 to the earlier of (1) the purchase from Hydro One of the M1 and M3 assets; or (2) a determination of the revised rate design they request in this proceeding.

Hydro One has two main responses. The first is that they are complying with the Board’s Distribution System Code, particularly Section 6.3.4. Secondly, Hydro One states that if these assets are sold, the Board should recognize precedents in the sale of similar assets to other utilities, particularly Oakville and Burlington. These sales, Hydro One states, have taken place at prices based upon commercial values.

Milton Hydro also asked the Board to clarify the basis on which utilities should value the purchased assets in their accounts. In particular, they wish to know whether it is only

the book value of assets that Milton Hydro has purchased that can be put in rate base and whether any additional compensation they are required to pay should be placed in the deferral account to be recovered from ratepayers as an expense.

Board Findings

The Board recognizes that where there is a pooling of costs in a customer class there will be winners and losers. Customers being served by long feeders with small loads will want to be billed on a per kilowatt hour basis and customers being served by short feeders that are heavily loaded like Milton will want to be billed on a per kilometre basis. The fact remains that in the situation here with very short feeders, Milton Hydro appears to be incurring charges that bear scant relationship to the cost.

The Board does not believe it appropriate to create a new definition of a dedicated user as suggested by Milton. This may have unintended consequences in other situations. Further, the Board will not require Hydro One to change the established definitions of any LV Lines.

While the issue in this proceeding is rate related, the dispute among the two parties expanded to the transfer price for the assets. Specifically, whether the assets should be sold to Milton and at what price. Milton would like to see the transfer at a book value while Hydro One wants a greater price similar to the Burlington transaction. If Hydro One prevails, there would be a significant profit to the benefit of the Hydro One shareholder. The purchasing utility on the other hand faces the difficulty that under the Board's existing rule, only the net value is generally allowed in rate base.¹⁶ This means a loss for the purchaser's shareholder

The Board believes that the simplest solution is to allow Milton to purchase the assets at book value. Hydro One recovered the cost of these facilities long ago.

Counsel for Hydro One has referred to the Burlington Hydro¹⁷ proceeding where the Board approved the sale of assets by Hydro One to that utility. The price agreed on, however, was higher than book value and included a commercial price as well as a premium to reflect foregone revenues.

¹⁶ RP-2005-0018 / EP-2005-0234 / EB-2005-0254 / EB-2005-0257

¹⁷ Transcript Vol. 7, p 42.

While it was not argued by any of the parties, it is not clear the Board has the authority to order Hydro One to sell assets at any specific price. Doing so may amount to expropriation and as the Supreme Court of Canada said in *ATCO*¹⁸, the ability to expropriate requires very explicit authority in the Statute. The Board does not have that authority. The only provisions in the Ontario Energy Board Act that relate to forced sales are Section 70.(13) which prohibits a licence condition requiring the disposition of assets and Section 59 which allows the Board to order that a distributor cede control of its system to another person. However, even in these situations, the original distributor continues to own the asset (see S.59.(10)).

The Board understands the concerns expressed by Milton. Any customer is entitled to just and reasonable rates and it is accepted that the rate must bear some relationship to the cost of servicing the customer. While the record in this case is far from complete on this issue the rate Milton is paying for this service does appear to be excessive. However, setting rates for individual customers is not a workable solution.

The preferred solution as indicated is for Hydro One to allow Milton to purchase these assets at book value. It appears that Hydro One is not prepared to do that or at a minimum is demanding a higher price and, as indicated, the Board is concerned that it may lack the jurisdiction to order Hydro One to proceed with the sale. In the circumstances, the Board strongly encourages Hydro One to proceed with the sale on the basis of the principles outlined. If that fails to occur within a time period for implementation before May 1, 2010, the Board directs Hydro One as part of its 2010 IRM to bring forward evidence relating to the construction of a rate specific to address Milton's circumstances.

Rate Harmonization and Bill Impacts

The greatest concern by intervenors in the area of cost allocation and rate design related to Hydro One's harmonization proposal and the resulting bill impacts.

Hydro One proposes to harmonize the rates for all of its customers in the 12 new customer classes over a four year period starting in 2008. As indicated above, Hydro One's customer base includes both Legacy and Acquired customers whose rates were

¹⁸ *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] 1 S.C.R. 140

previously segregated. Directionally, the Hydro One proposal seeks to combine customers with similar relevant characteristics in a homogeneous rate class, with the result that similar customers will pay the same rate.

The proposed rates are designed to recover the cost of servicing each class of customers as a whole. Hydro One states that the harmonization is appropriate as their accounting records are not segregated on an asset or expense basis for a legacy and acquired customers. That is; Hydro One has “one set of books”.

Hydro One selected the four year period for the purposes of harmonization for four reasons:

1. To limit the total bill impact for customers to 10% per year based on an average consumption for each class;
2. To coincide with the expected end date for the Board’s Third Generation IRM;
3. To coincide with the implementation of Hydro One’s new billing system; and
4. To coincide with the anticipated date for full implementation of commodity time of use rates.

The mitigation proposal limits the total bill impact to a maximum of 10% in 2008, 8% in 2009 and 7% in 2010 for customers with average consumption within each customer class. The mitigation proposal requires cross-subsidization within rate classes over the four year phase in period. Any shortfall in revenues from this mitigation will be absorbed first by the Acquired Distributors and, if that is not possible, then by the legacy customer classes in the same group as the acquired customer class.

The main criticism by the intervenors was that Hydro One’s assessment of customer bill impacts relates to only “average” customers and that the impact on the lower use “outlier” customers was not adequately addressed. A related complaint shared by CCC, CME, VECC and AMPCO was that Hydro One presented insufficient information regarding the impact on low use customers.

CCC submitted that Hydro One’s mitigation plan fails to consider the dollar impact to customers over the harmonization period. CCC rejects a mitigation proposal that is based exclusively on averages and percentages because outliers are not identified and alternative phase in periods were not considered. CCC concluded that the Board should defer approval of Hydro One’s harmonization proposal and direct Hydro One to provide

additional information on the outliers and require the Hydro One to develop options to address the adverse impacts on those outliers.

As CME noted, the customers most adversely affected are the customers of the former municipally owned utilities which Hydro One has acquired, the Acquired Distributors. Hydro One justified the rate increase that its harmonization proposal imposes on customers of Acquired Distributors on the grounds that they are being subsidized by the legacy customers. As stated earlier in this Decision, both CME and SEC questioned whether these customers really are being subsidized. They stated that it is equally possible that they have lower costs and the lower rates reflect those lower costs. CME noted that many of the utilities acquired by Hydro One are in more urban communities and may exhibit lower costs than those experienced in Hydro One's primarily rural system.

Hydro One responded that it has provided the Board and the intervenors detailed rate impact information. Hydro One recognizes that customers can experience significant percentage bill impacts at low monthly consumption. One example cited concerns nine customers in Woodville who consume less than 250 kw hours per month. For Woodville customers consuming 100 kw hours the rate impact was 27.6% or \$3.60 per month on the total bill. As Hydro One noted, the impact for low use customers is largely driven by the change in the fixed charge. While the impacts can be large on a percentage basis, the impacts are typically small in dollar terms.

Hydro One argued that its application meets the Board requirement to limit total annual bill impacts to 10% for an average customer. It further notes that the number of low use customers that will experience impacts greater than 10% a year is very low. Nonetheless, Hydro One recognized the concern expressed by the intervenors and offered two additional mitigation measures intended to limit the impact on low use customers:

- Acquired Residential customers with total bill impacts higher than 15% for 2008 would have the impact on their total bill limited to a maximum of \$3 per month. The mitigation would be in the form of a fixed dollar rebate based on the last actual annual billing data available, similar to the impact mitigation ordered by the Board in cases of transfer of customers to Hydro One as a result of eliminating Long Term Load Transfers.
- For Acquired General Service customers the total bill impact will be limited to the

higher of 15% and \$10 for Energy Billed customers and 15% and \$100 for Demand Billed.

The cost of this mitigation (revenue foregone and incremental costs associated with implementation of the plan) would be added to the proposed mitigation variance account.

Based on 2006 levels of consumption, Hydro One estimated that fewer than 300 Acquired Residential customers will consume less than 250 kWh per month in 2008 and have impacts higher than 15% or \$3 per month. These customers would receive a dollar credit on their bill to limit their bill impact to a maximum of \$3 per month.

Board Findings

The Hydro One mitigation proposal would limit the total bill impact to a maximum of 10% in 2008, 8% in 2009 and 7% in 2010 for those customers with average consumption within each customer class. The mitigation proposal requires cross-subsidization within rate classes in 2008 and over the four year phase in period. The Hydro One proposal meets the Board's general guidelines that rate increases in any one year should not be any more than 10% for the average customer.

The Board recognizes the concern by intervenors that low consumption customers will face rate increases significantly larger than this. While the rate increases on a percentage basis are large, the increases in dollar terms are relatively low.

Hydro One has responded to these concerns and introduced additional mitigation effects as outlined above which substantially reduced its concern. On this basis, the Board approves the mitigation proposal advanced by Hydro One.

The Board has considered expanding the harmonization plan over more than four years. This however does not assist low use residential customers; it simply allows additional time for acquired customers to pay back the subsidy they receive from legacy customers. For example, as shown in J.6.8 acquired customers moving to the R1 Class receive in 2008 a \$3.25 million dollar subsidy from legacy R1 customers. In 2009 and 2010 the acquired customers pay back \$1 million and \$1.6 million respectively to the R1 legacy customers.

Hydro One's proposed deferral account associated with its mitigation plan is dealt with later in this decision.

Deferral and Variance Account

Hydro One proposed to clear the balances of certain deferral/variance accounts and to establish three new deferral/variance accounts.

Balances and Disposition of Deferral/Variance Account

The December 31, 2007 overall balance in the respective deferral and variance accounts was originally estimated by the Company to be a net credit (payable to ratepayers) of \$30 million (including interest), which was updated during the hearing to a net credit of \$42.4 million. The April 30, 2008 overall balance was originally estimated by the Company to be a net credit balance of \$48.7 million, which was updated to a net credit balance of \$65.5 million. These balances include the smart meter variance account balances, accounts 1555 and 1556.

Hydro One requested that it be authorized to clear the forecast balances as of April 30, 2008 and to do so over a four year period starting May 1, 2008.

The updated April 30, 2008 balances, including interest, are shown in the table below. Also shown in the table are the December 31, 2007 balances, with interest to April 30, 2008. The smart meter balances have been shown separately from the subtotal of the other deferral/variance account balances.

Deferral/Variance Account Balances as at April 30, 2008			
Account Number	Description	Balance at December 31, 2007, Interest Improved to April 30, 2008 (\$ millions)	Balance at April 30, 2008, Including Interest and Principal to April 30, 2008 (\$ millions)
1508	OEB Costs Account	(0.2)	(0.2)
1592	Tax Changes Account	(6.3)	(7.2)
1580	RSVA Wholesale Market Services	(63.4)	(74.5)
1584	RSVA Tx Network & Tx Network Aggregation	6.6	(8.5)
1586	RSVA Tx Connection & Tx Connection Aggregation	7.5	3.8
1588 Sub-account Global Adjustment	RSVA Provincial Benefit	3.8	6.0
1550	RSVA Low Voltage	3.1	3.6
	Subtotal, before Smart Meter Balances	(48.9)	(77.0)
1555 and 1556	Smart Meter Minimum Functionality to May 31, 2007	5.9	7.0
	Smart Meter Minimum Functionality from June 1, 2007 to December 31, 2007 / April 30, 2008	(1.0)	2.3
	Smart Meter Exceeding Minimum Functionality to December 31, 2007 / April 30, 2008	1.1	2.2
	Subtotal, Smart Meter Balances	6.0	11.5
	Total Requested for Disposition	(42.9)	(65.5)

Board Staff submitted that the Board’s practice in the electricity sector is to only clear the latest available actual audited balances, plus carrying charges to the start of the new rate year – a credit of \$42.9 million in total in this case. Board staff also noted that the “large” difference between the original and the updated April 30, 2008 estimate suggests that forecasting the balances is difficult. Board staff submitted that disposition of the audited balances at December 31, 2007, would be consistent with the larger body of practice associated with electricity distributors and most 2008 cost of service decisions. However, Board staff also noted that forecasted principal balances were approved by the Board in Hydro One’s 2006 cost of service proceeding (RP-2005-0020 / EB-2005-0378).

Board staff also noted that because the Board is required to review the balance in Account 1588 each quarter, the Board has not cleared balances of the RSVA accounts in 2008 rate decisions for most other electricity distributors. Board staff noted that Article 490 of the Accounting Procedures Handbook does not classify Account 1550 (Low Voltage) as an RSVA and that the Board has cleared this account in most other 2008 rates decisions.

With respect to Account 1592 (Tax Changes), Board staff noted that the Board disallowed clearance of this account in the case of 2008 rates for Toronto Hydro in view of the combined proceeding that has been commenced to deal with tax matters pre April 30, 2006.

Board staff stated that it is unclear whether the Company applies interest on Account 1555 (Smart Meters). If it does, it should not as the amounts recorded already include a rate of return component.

Board staff also questioned why Hydro One does not use account 1588 to record line losses per the Board's previous directions.

With respect to the proposed four-year clearance, Board Staff suggested that a shorter clearance period might be more appropriate.

Intervenors supported the Company's proposal to use the April 30, 2008 balances and the time frame of the disposition.

Board Findings

In rate decisions for other distributors the Board has generally maintained the practice as noted by Board Staff. However, in addition to the exception noted by Board staff, there have been other exceptions to that general practice¹⁹. The exceptions were for a variety of reasons, unique to each case.

The unaudited net credit balance of April 30, 2008 is substantially larger than the audited December 31, 2007 balance. The Board agrees with intervenors that there are extenuating circumstances in this case that also warrant a departure from the general

¹⁹ For example, Hydro 2000 Inc. EB-2007-0704 and Toronto Hydro-Electric System Limited EB-2007-0680

practice. Despite rate mitigation, there will be substantial rate impacts on the acquired customers arising from harmonization and using the larger April 30, 2008 balances would further mitigate the impacts. Further, the Board sees merit in Board staff's suggestion to accelerate the disposition. This would reduce the initial rate impact and it would also lessen intergenerational inequity.

Accordingly, in the special circumstances presented in this case, the Board approves the disposition of the April 30, 2008 \$77.0 million net credit balance, which is listed as a subtotal in the above table and which excludes the smart meter variance account balances.

Consistent with its finding on the treatment of smart meter costs elsewhere in this decision, the Board also approves the disposition of the December 31, 2007 smart meter variance account balances, plus interest improvement to April 30, 2008, which represents a \$6.0 million net debit balance recoverable from ratepayers. In so finding, the Board is satisfied with the explanation by the Company in its reply argument that the manner in which it has applied carrying charges on the smart meter variance account does not constitute double counting.

The disposition of these balances shall be to the new rate classifications as proposed by Hydro One but the disposition shall be over a two year period, the starting date to coincide with the effective date of the new rates.

The Board has also noted that Board staff had questioned why the Company does not use account 1588 to record line loss variances per the Board's previous directions. As Hydro One pointed out, line losses is one of the settled issues, which the Board accepted. The Board therefore does not feel that this is the proceeding to deal with this issue raised by Board staff.

New Deferral Account

Hydro One requested Board approval for the following three new deferral accounts: Pension Cost Differential Account; OEB Cost Differential Account; and Bill Impact Mitigation Account.

Pension Cost Differential Account

In this account, Hydro One proposes to track the difference between forecast and the actuarially-determined pension obligations.

Some intervenors objected to the establishment of this account on the grounds that there is no regulatory precedent, that there is no such account for Hydro One's transmission business, and that the risk will be shifted from the shareholder to the ratepayer.

These intervenors, and Board staff, suggested that pension costs for 2008 be reduced by \$1.5 million to reflect the actuarial valuation filed with the Financial Services Commission of Ontario.

Hydro One argued that the deferral account will eliminate risk for both ratepayers and the shareholder and noted that there is a precedent, given that the Board had previously approved such an account for Hydro One Networks Transmission.

Board Findings

Pension obligations are common to all distributors. The Board's Accounting Procedures Handbook sets out the deferral accounts that all distributors may generally utilize without specific approval. A category for pension obligations is not on that list. In distributor-specific cases the Board has made exceptions to the general rule. In this case, given that a pension cost differential account has already been authorized by the Board for Hydro One Networks Transmission and these costs relate to personnel in the same corporate structure, it is reasonable to extend this regulatory treatment to Hydro One Networks. This account shall accrue interest at the Board's prescribed rate.

Since the updated actuarial valuation is already available, Hydro One shall reduce its forecast pension costs by \$1.5 million for purposes of setting 2008 rates and the adjusted pension costs shall form the reference value for purposes of the variance account.

OEB Cost Differential Account

This account would track the difference between the annual OEB Cost Assessments, intervenor cost awards, and costs associated with OEB-initiated studies and the amount for these expenditures approved by the Board as part of the 2008 distribution rates.

There was opposition by intervenors and Board staff to Hydro One's request on the grounds that there is no clarity as to what incremental costs may be recorded and that Hydro One would be receiving special treatment compared to other distributors.

Board Findings

As noted earlier, the Board's Accounting Procedures Handbook sets out the deferral/variance accounts that all distributors may generally utilize without specific approval. OEB cost variances is not on that list of accounts. The Board does not consider it reasonable in this case to exempt Hydro One from the Board's current policy not to authorize an OEB cost variance account to distributors.

Bill Impact Mitigation Account

This account would record the difference between the Company's revenue requirement and the application of the Company's revenue to cost ratios. The difference would arise from mitigating customer rate increases to specified levels. Hydro One's original mitigation proposal for these customers was estimated to result in a \$2.5 million annual revenue shortfall for the Company. Hydro One suggested that the balance would be recovered from all customers. As a result of the additional mitigation measures proposed in its reply argument, the account according to the Company would record "the revenue foregone and any incremental costs associated with implementing the additional mitigation measures".

AMPCO noted that, effectively, Hydro One is proposing that the R1 class should continue to be subsidized by other customer groups and then, via the proposed variance account, will receive a second subsidy when over 80% of the variance account is collected from other customers. Since the account is being established for the sole benefit of one clearly identifiable class of customers, the Board should confirm that any account balance that may be recoverable at a later date will be recoverable only from those same customers.

In VECC's view, it is the overall effect of all of the cost allocation and rate design changes that lead an under recovery of the Company's revenue requirement, not just from Rate 1. Therefore it is incorrect and misleading to characterize the need for the mitigation account as being associated with an under recovery by the R1 class.

Board Findings

No party has disputed the need for the mitigation account if the Board accepted the Company's harmonization proposal or a harmonization plan. The Board has accepted the Company's harmonization proposal with a mitigation mechanism as set out in the Company's reply argument. The Board authorizes Hydro One to establish the proposed mitigation account to record the costs of harmonization, including the incremental costs reasonably incurred for implementation.

Given the substantial discussion on the issue of who pays, it would be more efficient for the Board to make that decision now rather than wait for the time of disposition.

It is not reasonable that Hydro One should be burdened with any of the foregone revenue or the costs associated with the implementation of the mitigation plan. Neither would it be reasonable to only burden the customers for whom the mitigation is done in the first place. To do so would be a rate smoothing plan, not a mitigation plan. It would be reasonable in the circumstances that all Hydro One customers share in the costs of mitigation. At the first opportunity following the end of the implementation of the mitigation plan, Hydro One shall apply for disposition of the balance accumulated in the account, plus interest at the Board's prescribed rate, along with a proposed method for disposition of the balance in a manner that reflects the Board's findings in this decision.

4. Rate Implementation

On April 11, 2008 the Board declared Hydro One's 2007 rates interim as of May 1, 2008 and directed the Company to record in a variance account the difference between the 2008 Board approved revenue requirement and the revenue calculated using currently approved rates for the period from May 1, 2008 until such time as final rates are implemented.

This Decision will result in the approval of rates for the rate year commencing May 1, 2008. Further, the Board has made numerous findings throughout this Decision which would change the as-filed revenue requirement/deficiency claimed by Hydro One and would also necessitate certain rate riders. These are to be properly reflected in a Draft Rate Order incorporating an effective date of May 1, 2008 for the new rates and an implementation date of February 1, 2009.

Hydro One's current rates were declared interim as of May 1, 2008. Given the date of this Decision there will have been a difference between the revenue collected under the existing rates and the revenue that would have been collected if the new rates were implemented May 1, 2008. Hydro One was directed to record this difference in a variance account.

The Board orders that Hydro One will implement rate riders on its Service Charges and its Distribution Volumetric Rates from the implementation date to April 30, 2011, for the purpose of clearing this variance account. Hydro One will design a rate rider for each of the 12 classes that have been approved in this Decision to reflect the amounts by which actual revenues have fallen short or exceeded the revenues that would have been received from the respective classes if the approved distribution rates had been in effect from May 1, 2008.

The Board will accept a reasonable approximation to the respective surpluses and shortfalls associated with the respective classes within the variance account. Further, as the balance in the variance account may not be completely cleared by April 2011 Hydro One is authorized to record any remaining balances in a deferral account for disposition at a later time.

There is no need for the Company to design a rate rider with respect to its Retail Transmission Service Rates. Rather, the difference in such rates to the date of

implementation shall continue to be recorded in variance accounts 1584 and 1586 as appropriate.

In filing its Draft Rate Order for 2008 rates, the Company should attach appropriate documentation in support of its rates, disposition of deferral/variance accounts, disposition of other amounts, and the allocation of the approved revenue requirement to the rate classes. If any specific matter has not been dealt with for purposes of drafting the rate order to implement the new rates or dispose of the deferral/variance accounts, the Company shall clearly identify these in its filing.

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

1. The Company 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 25 days of the date of this Decision.
2. Intervenors may file with the Board and forward to the Company responses to the Company's Draft Rate Order within 32 days of the date of this Decision.
3. The Company shall file with the Board and forward to intervenors responses to any comments on its Draft Rate Order within 35 days of the date of this Decision.

A cost awards decision will be issued after the steps set out below are completed.

4. Intervenors eligible for cost awards shall file with the Board and forward to the Company their respective cost claims within 35 days from the date of this Decision.
5. The Company may file with the Board and forward to intervenors eligible for cost awards any objections to the claimed costs within 40 days from the date of this Decision.
6. Intervenors, whose cost claims have been objected to, may file with the Board and forward to the Company any responses to any objections for cost claims within 47 days of the date of this Decision.

The Company shall pay the Board's costs of, and incidental to, this proceeding upon receipt of the Board's invoice.

DATED at Toronto, December 18, 2008

ONTARIO ENERGY BOARD

Original Signed By

Gordon Kaiser
Vice-Chair & Presiding Member

Original Signed By

Paul Vlahos
Member

Original Signed By

Paul Sommerville
Member

APPENDIX A

HYDRO ONE NETWORKS INC.

2008 TEST YEAR

DECISION WITH REASONS

BOARD FILE NO. EB-2007-0681

LISTS OF PARTIES

**EB-2007- 0681
Hydro One Network Inc. –
2008 Distribution Rate Application**

List of Applicant and Intervenors

Updated – June 25, 2008.

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AND

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8. Hopper Foundry (1977) Ltd.	John R. Vickers Sales Manager Forest ON Tel: 519-786-2641 Fax: 519-355-7759 E-Mail: hoppfdry@xcelco.on.ca

Intervenors	Rep. and Address for Service
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10. Milton Hydro Distribution Inc.	Tom Brett Gowlings LLP Counsel 1 First Canadian Place 100 King Street West, Suite 1600 Toronto ON M5X 1G5 Tel: 416-369-4628 Fax: 416-862-7661 E-mail: tom.brett@gowlings.com
AND	Mary-Jo Corkum, CA Vice-President Finance Milton Hydro Distribution Inc. 55 Thompson Road South Milton ON L9T 6P7 E-mail: maryjocorkum@miltonhydro.com
11. Municipality of West Grey	Christine Robinson Chief Administrative Officer/Clerk 402813 Grey Road # 4 R. R. # 2 Durham ON N0G 1R0 Tel: 519-369-2200 Fax: 519-369-5962 E-mail: robinsonc@westgrey.com

Intervenors	Rep. and Address for Service
12. Ontario Power Generation	Tony Petrella Senior Advisor – Regulatory Affairs 700 University Avenue, H18-E1 Toronto ON M5G 1X6 Tel: 416-592-3036 Fax: 416-592-8519 Email: tony.petrella@opg.com
13. Pollution Probe Foundation	Jack Gibbons Public Interest Economics 625 Church Street, Ste. 402 Toronto ON M4Y 2G1 Tel: 416-926-1907 x 240 Fax: 416-926-1601 Email: jgibbons@pollutionprobe.org
AND	
Klippensteins Barristers & Solicitors	Murray Klippenstein 160 John Street, Ste. 300 Toronto ON M5V 2Es Tel: 416-598-0288 Fax: 416-598-9520 Email: murray.klippenstein@klippensteins.ca
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Intervenors	Rep. and Address for Service
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15. Power Workers Union (PWU)	John Sprackett Staff Officer, President's Office 244 Eglinton Avenue East Toronto ON M4P 1K2 Tel: 416-322-4787 Fax: 416-481-7914 E-mail: spracket@pwu.ca
AND	
Elenchus Research Associates (ERA)	Judy Kwik Senior Consultant 34 King Street East, Suite 610 Toronto ON M5C 2X8 Tel: 416-348-8777 Fax: 416-348-9930 E-mail: jkwik@era-inc.ca
AND	
	Bayu Kidane 34 King Street East, Suite 610 Toronto ON M5C 2X8 Tel: 416-348-0666 Fax: 416-348-9930 E-mail: bkidane@era-inc.ca
AND	

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16. Private Intervenor	Dave & Marguerite Morelatto 429 Morse Street Thunder Bay ON P7A 1G7 Tel: 807-624-1548 E-mail: dave_and_marguerite@shaw.ca
17. Rogers Cable Communications Inc.	Ian Mondrow Counsel MacLeod Dixon LLP Toronto Dominion Centre Canadian Pacific Tower 100 Wellington Street West, Suite 500 P. O. Box 128 Toronto ON M5K 1H1 Tel: 416-203-4435 Fax: 416-360-8277 E-mail: ian.mondrow@macleoddixon.com
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AND BDR North America Inc.	Paul Zarnett 34 King Street East, Suite 100 Toronto ON M5C 2X8 Tel: 416-214-4848 ext. 26 Fax: 416-214-1643 E-mail: pzarnett@bdrenergy.com
18. School Energy Coalition (SEC)	Jay Shepherd Counsel Shibley Righton LLP Barristers & Solicitors 250 University Avenue, Suite 700 Toronto ON M5H 3E5 Tel: 416-214-5224 Fax: 416-214-5432 E-mail: jay.shepherd@shibleyrighton.com
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AND	

Intervenor	Rep. and Address for Service
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AND	
Institutional Energy Analysis, Inc.	Rachel Chen Case Manager/ Consultant 250 University Avenue, Suite 700 Toronto ON M5H 3E5 Tel: 416-214-5218 Fax: 416-214-5418 E-mail: Rachel.chen@ieai.ca
19. Society of Energy Professionals, The IFTPE Local 160, AFL-CIO,CLC	Richard Long 425 Bloor St. E., Ste. 300 Toronto ON M4W 3R4 Tel: 416-979-2709 Ext. 2255 Fax: 416-979-5794 Email: longr@society.on.ca
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Intervenors	Rep. & Address for Service
21. Union Gas Limited	Pat McMahon Manager, Regulatory Research & Records 50 Keil Drive North Chatham ON N7M 5M1 Tel: 519-436-5325 Fax: 519-436-4641 Email: pmcmahon@uniongas.com
22. Vulnerable Energy Consumers Coalition (VECC)	Michael Buonaguro Counsel c/o Public Interest Advocacy Centre 34 King Street East, Ste. 1102 Toronto ON M5C 2X8 Tel: 416-767-1666 Fax: 416-348-0641 Email: mbuonaguro@piac.com
AND	Bill Harper Econalysis Consulting Services 34 King Street East, Ste. 1102 Toronto ON M5C 2X8 Tel: 416-348-0193 Fax: 416-348-0641 Email: bharper@econalysis.ca
23. Westcast Industries Inc.	Tony Thoma 150 Savannah Oaks Drive Brantford ON N3T 5L8 Tel: 519-750-000 ext. 1266 E-mail: tony.thoma@westcast.com

**EB-2007- 0681
Hydro One Network Inc. –
2008 Distribution Rate Application**

List of Applicant and Observers

Updated – June 25, 2008.

Applicant	Rep. and Address for Service
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	Applicant's Counsel
Rogers Partners LLP	D. H. Rogers 181 University Avenue Suite 1900 P. O. Box 97 Toronto ON M5H 3M7 Tel: 416-594-4500 Fax: 416-594-9100 E-mail: don.rogers@rogersmoore.com

Observers	Rep. and Address for Service
1. Bluewater Power Distribution Corporation	Leslie Dugas Manager, Regulatory Affairs 855 Confederation Street P. O. Box 2140 Sarnia ON N7T 7L6 Tel: 519-337-8201 Ext. 255 Fax: 519-332-3878 E-mail: ldugas@bluewaterpower.com

Observers	Rep. & Address for Service
2. Municipality of Grey Highlands	Kelley Coulter Chief Administrative Officer 206 Toronto Street South, Unit 1 Community Services Centre P. O. Box 409 Markdale ON N0C 1H0 Tel: 519-986-2811 Fax: 519-986-3643 E-mail: coulterk@greyhighlands.ca
3. Optimal Technologies (US), Inc.	Shawn Bayati Two Progress Plaza 100 East Davie Street, 19 th Floor Raleigh NC 27601 USA Tel: 919-459-9858 Fax: 919-334-6519 E-mail: shawnb@otii.com
4. Owen Sound, Council of the Corporation of the City	Glen E. Henry Director of Corporate Services Corporate Services Department 808 2 nd Avenue East Owen Sound ON N4K 2H4 Tel: 519-376-1440 Fax: 519-371-0511 E-mail: cityadmin@e-owensound.com
4. Waterloo North Hydro Inc.	Rene W. Gatien, P.Eng President & CEO P. O. Box 640 300 Northfield Drive East Waterloo ON N2J 4A3 Tel: 519-888-5554 Fax: 519-886-8592 E-mail: rgatien@wnhydro.com

APPENDIX B

HYDRO ONE NETWORKS INC.

2008 TEST YEAR

DECISION WITH REASONS

BOARD FILE NO. EB-2007-0681

SETTLEMENT AGREEMENT

Hydro One Networks Inc.

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483 Bay Street
Toronto, Ontario M5G 2P5
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Susan Frank

Vice President and Chief Regulatory Officer
Regulatory Affairs



BY COURIER

June 3, 2008

Ms. Kirsten Walli
Secretary
Ontario Energy Board
Suite 2700, 2300 Yonge Street
P.O. Box 2319
Toronto, ON.
M4P 1E4

Dear Ms. Walli:

EB-2007-0681 – Hydro One Networks' 2008 Distribution Rate Application – Settlement Proposal

A Settlement Conference was held in the matter of Hydro One Network's 2008 Distribution Rate Application from May 26 to May 30, 2008. The attached Settlement Proposal was developed and agreed upon by Hydro One and the 13 intervenors who participated in the settlement conference. Ten hard copies have been provided for the Board's reference and a text-searchable Acrobat version is being provided to the Board and intervenors today by email.

We would like to thank the Board's Facilitator, Mr. Chris Haussmann for effectively guiding the Settlement process, Board Staff for contributing to a fuller discussion on issues and the Intervenors for their proposals and timely responses to the Settlement Proposal Document.

Acceptance of the Final Settlement Proposal has been obtained via e-mail correspondence from all Intervenors.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank

c. EB-2007-0681 Intervenors
Mr. Rudra Mukerji
Ms. Jennifer Lea

Encl.

**Hydro One Networks Inc.
Test Year 2008 Distribution Rates
EB-2007-0681**

SETTLEMENT PROPOSAL

Preamble:

This settlement proposal is filed with the Ontario Energy Board (“the Board”) in connection with the application by Hydro One Networks Inc. (“Hydro One”) for an Order or Orders approving the revenue requirement and customer rates for the distribution of electricity to be implemented in 2008.

Further to the Board’s Procedural Order No. 3 dated and issued March 14, 2008, a settlement conference was held on May 26, 27, and 30, 2008 in accordance with the *Ontario Energy Board Rules of Practice and Procedure* (“Rules”) and the Board’s Settlement Conference Guidelines (“Guidelines”).

Hydro One and the following intervenors (“the parties”) participated in the settlement conference:

Association of Major Power Consumers in Ontario (“AMPCO”)
Canadian Manufacturers & Exporters (“CME”)
Consumers Council of Canada (“CCC”)
Electrical Contractors Association of Ontario (“ECAO”)
Energy Cost Management Inc. (“ECMI”)
Energy Probe Research Foundation (“EP”)
Green Energy Coalition (“GEC”)
Milton Hydro (“MH”)
Pollution Probe (“PP”)
Power Workers’ Union (“PWU”)
Rogers Cable Communications Inc. (“RCC”)
School Energy Coalition (“SEC”)
Vulnerable Energy Consumers Coalition (“VECC”)

Ontario Energy Board staff also participated in the settlement conference but are not party to this settlement proposal.

Outlined below are the positions of the parties following the settlement conference. The settlement proposal follows the format of the Approved Issues List for ease of reference. The issues are characterized as follows:

Settled: If the settlement proposal is accepted by the Board, the parties will not adduce any evidence or argument during the oral hearing as the Applicant and the intervenors who take any position on the issue agree to the proposed settlement.

Partially Settled: If the settlement proposal is accepted by the Board, the parties will only adduce evidence and argument during the hearing on portions of the issues as the Applicant and the intervenors who take any position on the issue were able to agree on some, but not all, aspects of the particular issue.

Not Settled: The Applicant and the intervenors who take a position on the issue will adduce evidence and argument at the hearing on the issue as the parties were unable to reach agreement.

For ease of reference, the following outlines the status of the issues as outlined in the settlement proposal:

Settled: Issue completely resolved. Parties will not adduce evidence or argument at the hearing.	Partially Settled: Issue partially resolved. Parties will adduce evidence and argument at hearing on certain portions of the issue.	Not Settled: Issue not resolved. Evidence to be adduced and argument presented on entirety of issue.
# issues settled: 17	# issues partially settled: 6	# issues not settled: 26

The positions taken by the various parties on each of the settled or partially settled issues are identified throughout the settlement proposal. A party who is noted as taking no position on an issue may or may not have participated in the discussion on that particular issue and takes no position on the settlement or partial settlement reached or on the sufficiency of the evidence filed to date.

The settlement proposal provides a brief description of each of the settled and partially settled issues, together with references to the evidence filed to date. The supporting parties each settled or partially settled issue agree that the evidence filed to date in respect of that settled or partially settled issue, as supplemented in some instances by additional information recorded in the proposal, supports the proposed settlement or partial settlement. In addition, the supporting parties agree that the evidence filed in support of

each settled or partially settled issue and the additional information as recorded herein contains sufficient detail, rationale and quality of information to allow the Board to make findings in keeping with the settlement or partial settlement reached.

The parties acknowledge that the Board may accept settlement on any individual issue, or combination of them.

The parties agree that all unsettled issues will be dealt with during the oral phase of this proceeding.

Unless stated otherwise, the settlement of any particular issue in this proceeding and the positions of the parties in this Proposal are without prejudice to the rights of parties to raise the same issue and/or to take any position thereon in any other proceedings.

Overview:

The parties were unable to reach agreement on several issues, including OM&A, capital programs, cost allocation and rate design including the Applicant's rate harmonization plan.

Many of the settled issues were issues that were canvassed during Hydro One's 2006 Distribution Rate Application, EB-2005-0378 and/or Hydro One's 2007/08 Transmission Rate Application, EB-2006-0501 and which the Board had previously approved or commented. The settlement proposal outlines references to the applicable Board Decision.

1. ADMINISTRATION (Exhibit A)

- 1.1. Has Hydro One responded appropriately to all relevant Board directions from previous proceedings?

Partially Settled. The parties agree that the Applicant has appropriately responded to all directives from prior proceedings including those from the 2006 Distribution rate application (EB-2005-0378) and the 2007/08 Transmission rate application (EB-2006-0501) as outlined in Exhibit A-17-1, Table 1 with exception of those directives related to the following:

- CDM
- Compensation

The narrowed scope of the issue is: “Has Hydro One responded appropriately to Board directions from previous proceedings with respect to CDM and compensation?”

Evidence:

A-17-1 Summary of Board Directives and Undertakings from Previous proceedings

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 1.2. Has Hydro One responded appropriately to the Board's Directions on CDM and Line loss reduction?

Partially Settled. The parties agree that the Applicant has responded appropriately to the Board's Direction on Line Loss reduction. The parties also agree that the remaining issue relating to Hydro One's response to the Board's Direction on CDM is covered under issue 1.1.

Evidence:

A-15-3 Distribution Line Loss

H-1-97, H-3-2, H-10-8, H-12-11

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

1.3. Are the Affiliate Service Agreements appropriate?

Settled. The parties agree that the Applicant's Affiliate Service Agreements are appropriate. They are similar in form and substance to those previously reviewed and approved in EB-2005-0378 and EB-2006-0501. However, the parties' agreement on this issue is without prejudice to the positions that they may take on the costs of Affiliate Services which fall within Issues 3.3 and 4.6.

Evidence:

A-8-3 Affiliate Service Agreements

H-1-92, H-10-2, H-12-1, H-12-2, H-13-28, H-13-29, H-13-30

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

1.4. Are Hydro One's Economic and Business Planning Assumptions for 2008 appropriate?

Settled. The parties agree that Hydro One's Economic and Business Planning Assumptions for 2008 are appropriate. In settling this issue, the parties relied upon information from Hydro One that changes in US exchange rate forecasts have no material impact upon its costs, that it has no debt issued in US dollars and has no current plans to issue any US dollar debt. The Applicant referenced Exhibit H-1-15 from proceeding EB-2005-0378, where it confirmed that the impact of an updated exchange rate on all US dollar payments during the year would not materially impact the test year revenue requirement.

Evidence:

A-14-2 Economic Indicators

H-7-17, H-7-18, H-7-19, H-10-19, H-11-1, H-11-2, H-11-3, H-11-4, H-12-3, H-12-6, H-13-1

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 1.5. Is the load forecast and methodology appropriate and have the impact of Conservation and Demand Management initiatives been suitably reflected?

Partially Settled. The Applicant continues to apply the same forecasting methodology as approved by the Board in EB-2005-0378. The only issues that the parties were unable to reach agreement on are the impact of CDM on the load forecast, the compatibility of Hydro One's load forecast with the OPA's load forecast and whether an LRAM is appropriate.

The narrowed scope of the issue is: "Have the impact of Conservation and Demand Management initiatives been suitably reflected in the load forecast? Is Hydro One's load forecast compatible with the OPA's load forecast? Is an LRAM appropriate at this time?"

Evidence:

A-14-3 Distribution Load Forecast and Methodology

H-1-17, H-1-101, H-1-102, H-1-103, H-1-104, H-1-105, H-1-106, H-1-107, H-1-108, H-1-109, H-1-110, H-2-1, H-2-2, H-2-21, H-7-20, H-10-3, H-10-4, H-10-5, H-10-6, H-11-5, H-11-6, H-11-7, H-11-8, H-11-9, H-11-10, H-12-4, H-12-5, H-12-7, H-13-38

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

1.6. Is service quality on the OEB specified performance indicators acceptable?

Settled. The parties agree that Hydro One's level of service quality in relation to OEB specified performance indicators is acceptable. The parties' agreement on this issue is without prejudice to any positions that may be taken regarding service quality targets as they relate to Issues 3 and 4.

Evidence:

A-15-1 Service Quality Indicators

H-1-43, H-1-44, H-1-45, H-1-46, H-1-47, H-1-48, H-1-53, H-1-54, H-1-58, H-6-1, H-7-21, H-7-22, H-7-23, H-11-11, H-11-12, H-12-8, H-12-9, H-12-10

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

1.7. Are the proposed Distribution Loss Factors appropriate?

Settled. The parties agree that Hydro One's proposed Total Loss Factors ("TLF") are appropriate. The proposed TLFs which are consistent with those approved by the Board in EB-2005-0378, are outlined below:

Proposed Customer Class	Proposed TLF %
Urban Residential	7.8
R1	8.5
R2	9.2
Seasonal	9.2
Urban General Service energy	9.2
Urban General Service demand	6.1
General Service energy	9.2
General Service demand	6.1
Street Light	9.2
Sentinel Lights	9.2
Distributed Generator	6.1
Sub-Transmission	3.4

The parties further agree that the TLFs shown above may need to be adjusted to reflect the Board's Decision relating to customer rate classes (Issue 7.1).

Evidence:

A-15-3 Distribution Line Loss, G1-10-1 Total Loss Factors

H-1-96, H-1-97, H-1-98, H-1-99, H-1-100, H-2-3, H-2-4, H-5-1, H-10-7, H-11-13, H-11-14, H-12-7, H-12-11, H-12-65

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

2. COST OF CAPITAL/DEBT (Exhibit B)

- 2.1. Is the proposed Capital Structure and Rate of Return on Equity for Hydro One's distribution business appropriate?

Settled. The parties agree that the capital structure and ROE proposed by Hydro One is appropriate. Hydro One is following the Board's deemed capital structure of 60% debt and 40% equity as approved in EB-2006-0501 and per the Board's direction in its report issued on December 20, 2006, *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors*. When implementing the Board's Decision in the establishment of final 2008 distribution rates, the Applicant will reflect the Board approved 2008 ROE for LDCs of 8.57%.

Evidence:

B1-1-1 Cost of Capital

H-1-111, H-1-112, H-12-12

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 2.2. Are Hydro One's proposed costs and mix for its short and long-term debt for the 2008 test year appropriate?

Settled. The parties agree that Hydro One's proposed costs and mix for its short and long term debt are appropriate. In settling this issue, the parties relied upon information from Hydro One that updating the long-term debt issues and cost rates with actual 2007 and 2008 debt issues and cost rates would have minimal impact on the revenue requirement. Further, Hydro One confirmed that when implementing the Board's Decision in establishing final 2008 distribution rates it will reflect the Board approved rates for deemed short-term debt of 4.47% and deemed long-term debt of 6.10% for the 2008 test year. The settlement is without prejudice to the ability of intervenors to advocate for updated long term debt costs in future rate proceedings.

Filed: June 3, 2008
EB-2007-0681
Exhibit L
Tab 1
Schedule 1
Page 10 of 26

Evidence:

B1-2-1 Cost of Third Party Long Term Debt, B2-1-1 Debt and Equity Summary,
B2-1-1 Cost of Long Term Debt

H-10-9, H-12-12, H-12-13, H-12-14, H-13-1, H-13-19, H-13-37

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

3. COST OF SERVICE (Exhibit C)

- 3.1. Are the overall levels of the 2008 Operation, Maintenance and Administration budgets appropriate?

Not settled. The parties were unable to reach agreement on this issue.

- 3.2. Is the 2008 vegetation management budget appropriate?

Not settled. The parties were unable to reach agreement on this issue.

- 3.3. Is the proposed level of 2008 Shared Services and Other O&M spending appropriate?

Not settled. The parties were unable to reach agreement on this issue.

- 3.4. Are the methodologies used to allocate Shared Services and Other O&M costs to the distribution business and determine the distribution overhead capitalization rate for 2008 appropriate?

Partially Settled. The parties agree that the methodology used by the Applicant to determine the distribution overhead capitalization rate for 2008 is appropriate. This methodology was approved by the Board at page 36 of their Decision in EB-2005-0378. The settlement of this issue was also accepted by the Board in proceeding EB-2006-0501.

The narrowed scope of the issue is: “Are the methodologies used to allocate Shared Services and Other O&M costs to the distribution business for 2008 appropriate?”

Evidence:

C1-5-1 Common Corporate Costs, C1-5-2 Overhead Capitalization Rate, C1-5-3 Common Asset Allocation

H-1-83, H-1-84, H-12-23, H-13-20

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 3.5. Is the proposed E-factor methodology and adjustment as part of the distribution overhead capitalization appropriate?

Settled. The parties agree that the Applicant's proposed E-factor methodology and adjustment as part of the distribution overhead capitalization is appropriate. In settling this issue the parties relied on information from the Applicant that the E-factor methodology is consistent with the Rudden overhead capitalization rate methodology that was accepted by the Board in EB-2005-0378. The 2008 E-factor adjustment represents a \$14.4 million one-time true-up of 2006 overheads capitalized. The Applicant confirmed that the E-factor adjustment did not result in an increase in the test year revenue requirement. Hydro One advised that in 2007 it initiated a more timely process by which overheads are reviewed and adjusted on a quarterly basis. This process improves the timeliness of the update mechanism within the approved Rudden methodology.

Evidence:

C1-5-2 Overhead Capitalization Rate

H-1-16, H-12-24

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 3.6. Are the 2008 Human Resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate?

Not settled. The parties were unable to reach agreement on this issue.

3.7. Is Hydro One's depreciation expense appropriate?

Settled. The parties agree that the Applicant's depreciation expense methodology is appropriate. Hydro One continues to employ the depreciation methodology approved by the Board at page 24 of their Decision in EB-2005-0378. The settlement of this issue was also accepted by the Board in proceeding EB-2006-0501. The parties agree that the actual amount of depreciation expense may be affected by the Board's Decision in respect of Issue 4, or other issues, and will be adjusted accordingly in establishing the final 2008 distribution rates.

Evidence:

C1-6-1 Depreciation and Amortization Expenses, C2-5-1 Depreciation and Amortization Expenses – Historic, Bridge Year and Test Year, D2-3-2 Continuity of Accumulated Depreciation

H-1-5, H-1-41, H-12-25, H-13-42

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

3.8. Are the amounts proposed for capital and property taxes appropriate?

Settled. The Applicant's methodology and tax calculations are accepted by the parties. The parties agree that the amount of property taxes is appropriate. When implementing the Board's Decision in the establishment of final 2008 distribution rates, Hydro One will use the prevailing capital tax rates applicable to the test year.

Evidence:

C1-2-7 Property Taxes, C2-4-1 Capital Taxes Test Year (2008)

H-1-93, H-12-3, H-13-39

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 3.9. Is the amount proposed for income taxes, including the methodology, appropriate?

Settled. The Applicant's methodology and tax calculations are accepted by the parties. When implementing the Board's Decision in the establishment of final 2008 distribution rates, Hydro One will use the prevailing income tax rates applicable to the test year.

Evidence:

C1-7-1 Payments in Lieu of Corporate Income Taxes, C2-6-1 calculation of Utility Income Taxes, C2-6-2 2006 Hydro One Networks Income Tax return

H-1-94, H-1-95, H-13-40

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 3.10. Is the level of Hydro One initiated and or delivered CDM activity and budget appropriate and should it be funded by OPA or in rates?

Not settled. The parties were unable to reach agreement on this issue.

- 3.11. Is the proposed spending on loss reduction efforts appropriate?

Settled: The parties agree that the proposed expenditures to reduce electricity system losses, as recommended in the Kinectrics study provided at Exhibit A-15-3, Attachment A are appropriate. The spending on line loss reduction initiatives recommended in this study, and already undertaken by Hydro One, are consistent with previously Board approved amounts. As such, Hydro One is not requesting any additional spending for specific loss reduction initiatives in the test year.

Evidence:

A-15-3 Distribution Line Loss

H-1-97, H-3-2, H-10-8, H-12-11

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

4. RATE BASE (Exhibit D)

4.1. Are the amounts proposed for Rate Base appropriate?

Not settled. The parties were unable to reach agreement on this issue.

4.2. Are the amounts proposed for 2008 Capital Expenditures appropriate?

Not settled. The parties were unable to reach agreement on this issue.

4.3. Are the 2008 sustaining capital expenditures proposed for Asset Replacement appropriate?

Not settled. The parties were unable to reach agreement on this issue.

4.4. Are the 2008 amounts proposed for Development capital appropriate?

Not settled. The parties were unable to reach agreement on this issue.

4.5. Is the 2008 budget for storm related capital expenditures appropriate?

Not settled. The parties were unable to reach agreement on this issue.

4.6. Is the proposed level of 2008 Shared Services and Other Capital expenditures appropriate?

Not settled. The parties were unable to reach agreement on this issue.

- 4.7. Are the methodologies used to allocate Shared Services and Other Capital expenditures to the distribution business and determine the Working Capital component of the Rate Base consistent with the methodologies approved by the Board in previous Hydro One rate applications?

Partially Settled. The parties agree that the methodology used by the Applicant to determine the Working Capital of \$273.2 million is consistent with the methodology approved by the Board at page 29 of their EB-2005-0378 Decision. This amount represents 11.2% of total OM&A and cost of power. The settlement of this issue was also accepted by the Board in proceeding EB-2006-0501.

The narrowed scope of the issue is: “Are the methodologies used to allocate Shared Services and Other Capital expenditures to the distribution business consistent with the methodology approved by the Board in previous Hydro One rate applications”.

Evidence:

D1-1-3 Working Capital and Lead/Lag

H-1-11

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

- 4.8. Does the Asset Condition Assessment information adequately address the condition of the distribution system assets and support the OMA and Capital expenditures for 2008?

Settled. The parties agree that the Asset Condition Assessment information filed by the Applicant adequately addresses the condition of the distribution system assets. The parties agree that the extent to which the Asset Condition Assessment information supports the OM&A and capital expenditures will be dealt with as part of Issues 3.1 and 4.2 respectively.

Evidence:

D1-1-2 Distribution Assets, D1-2-1 Asset Condition Assessment and Analysis

H-1-14, H-1-55, H-7-1, H-12-26, H-12-27, H-13-8, H-13-43

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC,

- 4.9. Are the proposed capital expenditures to reduce electricity system losses appropriate?

Settled: The parties agree that the proposed capital expenditures to reduce electricity system losses, as recommended in the Kinectrics study provided at Exhibit A-15-3, Attachment A are appropriate. The capital spending on line loss reduction initiatives recommended in this study, and already undertaken by Hydro One, are consistent with previously Board approved amounts. As such, Hydro One is not requesting any additional capital spending for specific loss reduction initiatives in the test year.

Evidence:

A-15-3 Distribution Line Loss Study, D1-3-5 Shared Service and Other Capital

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

5. REVENUE REQUIREMENT (Exhibit E)

5.1. Is the calculation of the proposed revenue requirement for 2008 appropriate?

Settled. The parties agree that the calculations for revenue requirement are appropriate. However, the final amount of revenue requirement will reflect the Board Decision.

Evidence:

E2-1-1 Calculation of Revenue Requirement (2008)

H-10-25, H-10-26, H-12-32

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

5.2. Is the proposed amount for 2008 External Revenues, including the methodology used to cost and price these services, appropriate?

Settled. The parties agree that the proposed amount for 2008 External Revenues, including the methodology used to cost and price these services is appropriate.

ECAO's agreement on this issue is premised on clarification from Hydro One that: i) the streetlight maintenance revenues referred to in the pre-filed evidence [Exhibit E3, Tab 1, Schedule 1, page 10, line 13] consists of approximately \$50,000 from services provided as a "service provider of last resort" to 12 Municipalities and First Nations primarily located in northern Ontario where no other qualified contractors are available, or willing, to provide the service; ii) the sentinel lighting service revenues arise solely from customers to whom Hydro One is required to provide the service pursuant to Ontario Regulation 161/99 [s.5(6)]; and iii) the design and redesign of new subdivision services provided to developers relates to design and redesign of the Hydro One owned distribution network within the subdivision, and redesigns are included in the "external work" category by virtue of the cost recovery nature of the work.

ECAO's and the Applicant's agreement on this issue is expressly without prejudice to either party with respect to characterization in the pre-filed evidence of those elements of new connection and upgrade service work as "work that must be done by Hydro One Distribution under its Distribution Licence" [Exhibit E3, Tab 1, Schedule 1, page 8, lines 13 through 19].

Evidence:

E3-1-1 External Revenues, E3-2-2 External revenues Historic, Bridge Year and Test Year

H-10-26, H-12-33, H-12-34

Supporting Parties: AMPCO, ECAO, EP, CCC, CME, PWU, SEC, VECC

Parties taking no position: ECMI, GEC, MH, PP, RCC

- 5.3. Is the proposed accounting treatment of non utility revenue and expenditures associated with OPA funded CDM appropriate?

Not settled. The parties were unable to reach agreement on this issue.

6. REGULATORY ASSETS (Exhibit F)

- 6.1. Is the proposal for the amounts, disposition and continuance of Hydro One's existing Deferral and Variance Accounts (Regulatory Assets) appropriate?

Not settled. The parties were unable to reach agreement on this issue.

- 6.2. Is the proposal to establish new Deferral and Variance Accounts appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7. COST ALLOCATION AND RATE DESIGN (Exhibit G)

7.1. Are Hydro One's proposed new Customer Rate Classes appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.2. Is Hydro One's cost allocation appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.3. Are Hydro One's proposed rates appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.4. Are the proposed revenue to cost ratios appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.5. Are the fixed-variable splits for each class appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.6. Is Hydro One's proposal to have both fixed and variable service charges for sub-transmission customers, sentinel lights and street lights appropriate?

Partially Settled: The parties agree that the Applicant's proposal to include both fixed and variable components for the service charges applicable to sentinel light and street light rate classes is appropriate.

The narrowed scope of the issue is: Is Hydro One's proposal to have both fixed and variable service charges for sub-transmission customers appropriate?

Evidence:

G1-4-2 Target rates for Retail Customers, G1-4-4 Rate Considerations for Sub-Transmission Customers

H-12-42, H-12-46

Supporting Parties: AMPCO, ECMI, EP, CME, VECC

Parties taking no position: CCC, ECAO, GEC, MH, PP, PWU, RCC, SEC

7.7. Is the proposal for harmonization of rates appropriate?

Not settled. The parties were unable to reach agreement on this issue.

7.8. Are the customer bill impacts resulting from the proposed rate impact mitigation plan reasonable?

Not settled. The parties were unable to reach agreement on this issue.

7.9. Are the proposed Retail Transmission Service Rates appropriate?

Settled: The parties agree that the Retail Transmission Service Rates are appropriate. These Rates have been determined using the current Board approved methodology outlined in Chapter 11 of the Distribution Rate Handbook and using the Ontario Uniform Transmission rates (EB-2007-0759), effective November 1, 2007, as approved by the Board in their Decision.

Evidence:

G1-6-1 Retail Transmission service Rates, G2-4-1 Retail Transmission Services Rates Details

H-1-159, H-1-160, H-1-161, H-1-162, H-1-163, H-12-60

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

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7.10. Is the proposal for regulatory asset rate rider #3 appropriate?

Not settled. The parties were unable to reach agreement on this issue.

8. SMART METERS

8.1. Is the 2008 smart meter O&M budget appropriate?

Not settled. The parties were unable to reach agreement on this issue.

8.2. Is the proposed 2008 capital spending for the Smart Meter program appropriate?

Not settled. The parties were unable to reach agreement on this issue.

8.3. Are the amounts for Smart Meter related variance accounts appropriate?

Not settled. The parties were unable to reach agreement on this issue.

8.4. Is the treatment of stranded meter costs appropriate?

Settled: The parties agree that the Applicant's treatment of stranded meter costs is appropriate. In the Applicant's 2006 Distribution Rate Application, a comprehensive depreciation study prepared by Foster Associates was filed dealing with all of Hydro One's assets (Exhibit C1, Tab 7). Intervenors did not cross examine on the study and no witness testified about the study. As a result, on page 24 of its Decision in EB-2005-0378 the Board accepted the costs flowing from the study.

As it relates to stranded meters, the depreciation study stated:

“It is the opinion of Foster Associates that a responsible and appropriate treatment of the embedded base of conventional meters (i.e., Account 1860) is amortization over a period of 5 years. The recommended amortization period is consistent with the Provincial initiative to replace all conventional meters by 2010.”

The Applicant continues to follow the same depreciation treatment of stranded meters that was implemented following the Board's Decision in EB-2005-0378.

Evidence:

C1-6-1 Depreciation and Amortization Expenses

Supporting Parties: AMPCO, EP, CCC, CME, SEC, VECC

Parties taking no position: ECAO, ECMI, GEC, MH, PP, PWU, RCC

8.5. Is Hydro One's regulatory treatment of Smart Meter costs appropriate?

Not settled. The parties were unable to reach agreement on this issue.

APPENDIX C

HYDRO ONE NETWORKS INC.

2008 TEST YEAR

DECISION WITH REASONS

BOARD FILE NO. EB-2007-0681

INTERIM RATE ORDER DATED APRIL 11, 2008

Ontario Energy
Board

Commission de l'Énergie
de l'Ontario



EB-2007-0681

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
Networks Inc. for an order approving or fixing just and
reasonable rates and other charges for the distribution of
electricity.

BEFORE: Gordon Kaiser
Presiding Member

Paul Sommerville
Member

Paul Vlahos
Member

DECISION AND ORDER ON INTERIM RATES

Hydro One Networks Inc. (“Hydro One” or the “Company”) filed an application, dated December 18, 2007, with the Ontario Energy Board under section 78 of the *Ontario Energy Board Act*, S.O. 1998, c.15, Schedule B, for an order or orders approving and fixing just and reasonable rates for the distribution of electricity, to be effective May 1, 2008.

By way of a letter dated February 27, 2008 Hydro One requested that its existing 2007 rates for the distribution of electricity approved under the proceeding EB-2007-0542, be

declared interim effective May 1, 2008. Hydro One also proposes to establish a variance account to record the difference between the 2008 Board approved revenue requirement and the revenue calculated using currently approved rates for the period from May 1, 2008 until such time as new rates are implemented. The Company proposes that the balance in this account be cleared by means of a rate rider, in accordance with direction from the Board on the disposition of this account. This amount, the Company proposes, be reduced by the continued collection of Rate Rider #1 (an existing rate rider) over the same period.

On March 14, 2008, the Board issued Procedural Order No. 3, which set out the dates for filing written submissions on the Company's request. The Board received submissions from the School Energy Coalition ("SEC"), Association of Major Power Consumers in Ontario ("AMPCO"), Energy Probe Research Foundation, Green Energy Coalition, the Power Workers Union, Vulnerable Energy Consumers Coalition ("VECC") and Board staff.

SEC supports the Company's request for interim rates, however submits that the method of rate recovery be decided after the evidentiary portion of the hearing is concluded. Similarly, VECC supports the request, with the proviso that such an order is without prejudice to the Board's determination of the effective date of the Board's rate order in this proceeding. Board staff submits that the component of Hydro One's 2008 rate application dealing with the transmission-related charges it proposes to apply to its embedded distributor customers, be approved on an interim basis. AMPCO wishes the same for Direct customers and also requests the immediate clearing of the related variance account.

The Company does not support the request to make the proposed Retail Transmission Service ("RTS") rates to Embedded Local Distribution Companies ("LDC") and Direct customers interim. The Company argues that the implementation of a rate change for one class of customers would be unfair to the balance of Hydro One's customers who

would continue to pay the current RTS rates until new rates are approved by the Board. In response to APMCO's proposal for the immediate disposition of the variance accounts, Hydro One submits that the variance account mechanism ensures that customers are held whole regardless of when RTS rates are implemented and therefore it is premature to dispose of the balances at this time.

Findings

The processing of Hydro One's 2008 rates application has not yet concluded and based on the current schedule for the proceeding, it will not result in a final rate order for implementation by May 1, 2008. The Board also notes that there is general support for Hydro One's request from the parties that responded.

The main concern expressed by Board staff and AMPCO relate to the timing of the implementation of the proposed new RTS rates to Embedded LDCs and Direct customers and the timing of the clearing of the regulatory asset balances.

On October 17, 2007, the Board issued its EB-2007-0759 Rate Order, setting new Uniform Transmission Rates for Ontario transmitters, effective November 1, 2007. The Board approved a decrease of 18% to the wholesale transmission network rate, a decrease of 28% to the wholesale transmission line connection rate, and an increase of 7% to the wholesale transformation connection rate. The combined change in the wholesale transmission line connection and transformation connection rates amounts to a reduction of 5%. The Board notes that in other decisions recently issued for electricity distributors' rates, effective May 1, 2008, it directed distributors to reduce their RTS rates to reflect this reduction in the Uniform Transmission Rates.

AMPCO submitted that the same rate reduction should be applied to Direct customers and requested the immediate clearing of the related variance account. The Board notes that the Direct customers are not the same as embedded distributor customers, despite the fact they are grouped together in the proposed Sub-Transmission Class. The

embedded distributors have been ordered by the Board to reduce their retail transmissions rates through which they recover from their own customers the charge imposed by Hydro One. An interim reduction in the RTS rates charged by Hydro One to the embedded distributors should reduce the level in the variance accounts that these distributors carry. Direct customers are end-use consumers and therefore do not pass the retail transmission rate charge through to any other user, and do not have variance accounts. The Board will not grant AMPCO's request, but will reduce the RTS rate charged to embedded distributors.

The Board orders that, except for the component of Hydro One's rates dealing with transmission-related charges it applies to its embedded distributors as noted below, and pending the issuance of final rates for 2008, the existing 2007 rates approved under proceeding EB-2007-0542 be declared interim as of May 1, 2008.

The Board orders that, the component of Hydro One's 2008 rate application (EB-2007-0681) dealing with the transmission-related charges it proposes to apply to its Embedded LDCs, as shown in Exhibit G2, Tab 94 Schedule 1 page 3 of 8, be declared to be interim rates for these customers as of May 1, 2008.

The Board will allow Hydro One to record the difference between the 2008 Board approved revenue requirement and the revenue calculated using currently approved rates for the period from May 1, 2008 until such time as final rates are implemented in a variance account, the disposition of which will be decided when the Board issues its decision in this proceeding.

In granting this request, Hydro One should be aware that the action of granting interim rates should in no way be construed as predictive, in any degree, of the final determination of this application. The Board will consider the effective date of its decision when it renders the final decision.

DATED at Toronto, April 11, 2008

ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary