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BY COURIER

April 8, 2009

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

EB-2008-0272 – Hydro One Networks' 2009-2010 Transmission Revenue Requirement Application – Reply Argument

Attached are 10 copies of Hydro One Networks reply argument.

An electronic version has been submitted through the Board's Regulatory Electronic Submission System and the proof of successful submission is also attached.

An electronic copy has been forwarded to EB-2008-0272 intervenors.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank

Attach.

c. EB-2008-0272 Intervenors

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Hydro One is pleased to file its reply argument in relation to its transmission Application EB-2008-0272. This document is complementary to the oral argument presented on March 6, 2009 by Hydro One to the OEB. The intent of this reply is to respond in some detail to the arguments of the OEB Staff and Intervenors. The intent is not to summarize or repeat the vast body of evidence which has already been put forth.

Hydro One received final argument submissions from the OEB Staff and the following Intervenors:

- Association of Major Power Consumers of Ontario (AMPCO)
- Building Owners and Managers Association of the Great Toronto (BOMA) and The London Property Management Association (LPMA)
- Canadian Manufacturers & Exporters (CME)
- Consumers Council of Canada (CCC)

- Electricity Distributors Association (EDA)
- Energy Probe (EP)
- Lewis Balogh (LB)
- Pollution Probe (PP)
- Power Workers Union (PWU)
- School Energy Coalition (SEC)
- The Society of Energy Professionals (SEP)
- Vulnerable Energy Consumers Coalition (VECC)

The intervenors have raised a large number of disparate issues, many of which were neither raised by them in the stakeholder sessions, the multitude of written interrogatories, nor the oral phase of the hearing. As a result, it is difficult to address many of the issues raised as there is no evidentiary basis on which the Board could base a decision.

The Applicant will do its best to direct the Board to the evidence, where it exists, in the arguments to follow. However, before doing so, Hydro One would like to address several general issues common to a number of intervenors. Hydro One will address these general issues first, followed by its response to specific issues in accordance with the Issues List.

Preliminary Issues

Impact of the Economy on the current application

Ontario and indeed the world are currently in the midst of a state of economic downturn. Jobs have been lost, markets are down and economic indicators are poor. As Hydro One anticipated in its Argument in Chief, this current state of affairs has emerged as a common theme in many intervenor arguments. Intervenors have urged the Board to reduce the Applicant's proposed spending and its capital projects because of the current downturn in the economy, ignoring the system performance implications.

Hydro One submits that it would be inappropriate for this Board to do so, as it stated in its Argument in Chief.

Hydro One has filed a full cost of service application to establish its revenue requirement and rates for 2009 and 2010. Hydro One witnesses acknowledged during the oral hearing that since the business planning process began, and since its application was filed, economic indicators have changed. Hydro One believes that the effect of updating all the evidence would be to increase rates, in large part due to the decline in the load forecast. Nevertheless, Hydro One has decided to base its revenue request on the basis of the Application as filed.

While it is obviously relevant for the Board to consider current economic conditions, it would be inappropriate to artificially suppress rates and curtail necessary capital projects and other programs simply because the economy is currently not doing well.

As the Board well knows, Hydro One's objective is to provide safe and reliable transmission service to its customers. While obviously the utility is obligated to provide that service in an efficient and cost effective way, it must also be given a reasonable opportunity to earn its allowed rate of return and maintain its financial integrity.

Those representing intervenor groups should remember that the transmission system exists for its customers. It is important to customers that the transmission system is properly maintained and expanded to meet current and future needs. Hydro One understands and accepts that it has a heavy responsibility as the Province's major transmission system provider. It must provide this crucial service in a way that is safe and reliable. But this has a cost, and as a result, the company is going through a period in its evolution when the costs are rising. The relevant question is '*are there valid reasons* *to show why costs are rising?*'. The Applicant submits that it has provided a full explanation for the proposed spending in its pre-filed evidence, the interrogatory process and the oral hearing.

Hydro One is a stand alone public utility with operations structured like any private, for profit corporation. Hydro One is incorporated under the Ontario Business Corporations Act. It provides an essential service to the people and businesses of Ontario. Hydro One is legally obligated, regardless of the state of the economy, to ensure that it provides a safe, efficient and reliable transmission system that meets the present and future needs and demands of the province.

In meeting its mandated obligation, Hydro One must look ahead and plan on a steady and consistent basis. Its capital projects are large and complex and tend to have long lead times. The maintenance of the system must be managed with a steady, constant hand. This planning cannot be stopped and started with every shift in the economy. When this recession ends, the transmission system must be properly sized and maintained. The Applicant cannot wait until the economy improves to undertake needed sustainment and development projects.

The transmission system should not be used as a vehicle to address much broader economic problems. Even if the Board had the mandate to do so, there is no evidence in this case to demonstrate that the policy proposed by intervenors would be a good one. As outlined in the Argument in Chief, it is submitted that this Board, as an economic regulator, must ensure that the interests of the Company and its customers are balanced and that the utility does not exploit its monopoly position to its own advantage. It is not the role of those of us involved in the regulatory process to artificially manipulate electricity rates in a misguided effort to offset a province-wide, country-wide, and world-wide recession.

Hydro One notes it has taken steps to ensure ratepayer impact is minimized to the extent possible, in light of the extensive work programs and projects that the Company believes it must undertake. Hydro One notes that it is requesting that rates be effective July 1, 2009, instead of January 1, 2009, which is likely to the detriment of the shareholder. By not updating the evidence for the 2009 and 2010 test years Hydro One has:

1. Foregone lost revenues as a result of a lower load forecast as noted by Mr. But of approximately $9 million for 2009 and $14 million for 2010 [Tr. Vol. 5, pg. 72];
2. Not reflected increased third party long-term debt costs as described by Mr. Cowan [Tr. Vol. 5, pg. 31]; and
3. Not updated program expenditures for additional projects identified since the budget was finalized as noted by Mr. Graham [Tr. Vol. 1, pg. 110] and Mr. Van Dusen [Tr. Vol. 3, pg. 163] and in response to Interrogatory I.1.10.

In addition, Hydro One has chosen to request a deferral account for pre-IPSP OM&A development work rather than expensing these amounts when incurred. The Company has clearly taken steps to minimize expenditure impacts to ratepayers during these recessionary times and the Board must balance intervenor concerns with the work programs that must be undertaken. If the Board approves the application as filed, the total bill impact to the average customer would be 0.5% in 2009 and 0.9% in 2010. The update for new Cost of Capital parameters and income tax rates will further reduce the level of these increases.

It is therefore submitted that Hydro One's application and various proposals, such as the capital projects proposed, must be assessed on the evidence before the Board. If the justification for the project exists and the Board is satisfied with the evidence, then Hydro One submits those projects ought to be approved. It would be inappropriate to disallow necessary projects simply due to the state of the economy.

Envelope Reductions:

As in prior proceedings, a number of intervenors have urged the Board to consider envelope, percentage or dollar reductions to capital and other programs, without any evidentiary basis for doing so.

For example, SEC has compared proposed increases in sustaining, development and operations OM&A with inflation of 3%, without any meaningful criticisms of the underlying causes of the proposed increases.

CME, along with BOMA and LMPA, have urged a 10% reduction in capital and a global reduction in the OM&A. Again, there has been no constructive challenge to the evidence supporting the need for the work programs, beyond the assertion that the proposed spending is simply too high.

Some intervenors have urged the Board to reduce OM&A levels based on the misleading argument that Hydro One's costs are increasing on a "$ per line Km" and a "$ per TWh" basis. This type of analysis is not useful nor in keeping with the evidence filed in this proceeding. The primary driver for increasing OM&A costs is the deteriorating performance and asset condition associated with many of Hydro One's aging station assets as discussed under Issue 3.1. Increased spending on maintaining asset performance does not affect the total Km of line owned by Hydro One nor does it impact the TWh transmitted. Thus, increasing costs related to asset maintenance, with no corresponding increase in the comparison denominator erroneously suggests a deteriorating trend in efficiency. Hydro One thus urges the Board to view with caution this selective use of performance metrics without consideration of the underlying facts.

Selective use of statistics and mere comparisons of either dollar or percentage increases can be misleading. The company does recognize that large dollar or percentage increases need to be supported by solid evidence. It is for that reason that the company has explained the need for these increases and filed extensive evidence to explain why they are necessary.

An illustrative example of the danger in using simple dollar or percentage increases may assist. The applicant is currently seeking a revenue requirement of $1,230 million for 2009 and $1,341 million for 2010. This is only a 5.8% and 15.3% increase respectively from the Board approved revenue requirement of $1,163 million in 1999, 10 years ago. The requested increase is less than the rate of inflation over the same time period.

Of course the applicant does not seek the Board's approval on that basis as it would be unreasonable and contrary to the principles of rate making to do so. However, Hydro One submits that the example is illustrative of the weakness in the approach taken by intervenors when urging the Board to make envelope reductions without a compelling challenge of the evidence adduced in support of the increases.

Business Planning Process:

A number of intervenors have criticized Hydro One's business planning and budget process. Indeed this was a key area of focus during the oral portion of the hearing. Intervenors have used those criticisms to support their positions that work programs must be arbitrarily slashed as a result.

Hydro One believes in the integrity and rigour of its business planning process. The final result of that process is before the Board in this application. The process to achieve that final result was long, intensive and involved numerous individuals from all of the lines of business.

In response to intervenor requests during the stakeholdering process, through the interrogatory phase of the hearing and during the oral phase of the hearing, Hydro One has done its best to provide intervenors and the Board with sufficient evidence so that all interested parties have confidence in the process.

The utility's good faith effort in this regard has only resulted in further criticism and unwarranted attacks.

VECC submitted that both the Board and other parties require more information regarding the workings of Hydro One's planning process including the basis for the "minimum spending level", the prioritization of project/work activities and the residual risk associated with the alternative levels of spending considered. VECC seeks the Board to direct Hydro One to provide this level of detail in its next rate filing.

Hydro One disagrees. Hydro One has, since it came before the Board with its first distribution rate application, been open with intervenors and the Board about its business planning process. Since then, Hydro One has been responsive to requests for additional information and evidence. Hydro One has filed extensive additional pre-filed evidence in this current case to ensure the Board has the necessary information to render an informed decision respecting requested spending levels.

In addition to evidence describing the Planning Process [A.14.1], the Investment Prioritization Process [A.14.5], Project and Program Approval and Control [A.14.6], Hydro One filed two new exhibits: [A.14.4] "Investment Plan Development, which described in detail the investment plan development process for Sustaining, Development and Operations OM&A and Capital programs and [A.14.7] "Work Execution Strategy", which detailed all the steps Hydro One has implemented to ensure the increased work requirements are achieved. In addition, the specific OM&A and Capital expenditure exhibits [C1.2.2 – C1.2.4, D1.3.2 – D1.3.4] were greatly expanded to provide more detail on the development and need for Sustaining, Development, Operations program expenditures.

During the oral part of the proceeding, in addition to extensive cross-examination of all four Hydro One witness panels respecting the budget planning process, further documentation was provided through the provision of the confidential Hydro One Board Memorandums [I.4.2, KX3.4, KX3.5] and through the filing of Undertaking J2.7 and Exhibit K3.2. Undertaking J2.7 presented the minimum capital and OM&A expenditure levels at the beginning of the planning process compared to the final expenditure levels sought for recovery in this Application. Exhibit K3.2 shows the results from three of many iterations undertaken in the finalization of the test year budgets.

VECC's request for even more information on each iteration in the process crosses the line into micro-management of Hydro One's affairs and is unduly intrusive.

CME argues that the sheer magnitude of Hydro One's budgeted increases in capital and operating spending for 2009 and 2010 calls Hydro One's business planning and budgeting process into question. CME questioned the rigour of the planning process.

CME is incorrect. The utility's business planning process is sophisticated and disciplined. It undergoes several iterations, all with a view to balance the interests of the shareholder and the ratepayers, while maintaining the paramount duty of providing a safe, efficient and reliable transmission system, consistent with government policy directives. This balancing act is not an easy task. Hydro One notes that no intervenor has suggested how the business planning process could be improved. Rather, arbitrary reductions are urged. Hydro One asks the Board to reject those arguments.

Hydro One has filed extensive evidence in support of its application and in defence of its business planning process. It has done its best through extensive stakeholdering and expanded evidence to explain its planning process to those who are truly interested. Hydro One submits that its planning process is rigorous and effective and the Company is hopeful that the Board will agree.

Changing Electricity Environment

The past several years have seen significant changes for the electricity sector in Ontario pursuant to various government directives. The transmission system is not immune from the impact of these changes. The applicant, this Board and indeed intervenors are not strangers to these changes which include an ongoing shift to cleaner energy and conservation and demand management activities and the announced target to eliminate coal fired plants.

At the outset of this hearing, Hydro One indicated that the Green Energy Act would not have an impact on the present application. Hydro One intended to convey that the application, as filed, ought to proceed as changes arising from the Green Energy Act remain unknown and are unrelated to the Company's proposals which are currently before the Board.

On the day this hearing began, the Minister of Energy and Infrastructure, Mr. Smitherman, when introducing the Green Energy Act explained that the Act would accelerate bringing renewable energy to Ontario and would continue the development of a culture of conservation in Ontario. In addition, Mr. Smitherman stated:

> "Working proactively with our energy agencies we would initiate investments in the development of new transmission capacity, and the Act would replace the snail's pace with sense of urgency…
>
> …because all energy consumers would reap the benefits of an improved energy system, we want to recognize that our investments in certain initiatives and programs that would be made possible by this legislation would be borne through energy rates".

Hydro One expects that it will be required to further expand the transmission system in the future to fulfill the mandate of the Green Energy Act. That said, the capital and other programs put forward in this Application are a necessity. Hydro One is unlikely to be in a position to respond to these anticipated government policy directives without first completing the capital plans contained in this Application.

Finally, CCC in their argument suggests that Hydro One's Application raises a number of questions about the Board's ability to determine whether the proposed expenditures are prudent given Hydro One's assertions that many of its expenditures are required in order to satisfy the requirements of the Ontario Power Authority ("OPA").

Ultimately it is the Board which makes the final decision as to whether a specific project is prudent and the need justified. It is the Board that determines if capital projects and associated expenditures are approved for inclusion in rate base, not the OPA. The Board will make its decision as to project need in one of three ways: either through their review and approval of the OPA's Integrated Power System Plan, upon the evidence presented in either this rate application or a subsequent rate application, or at the time of rendering approval of a specific transmission line application as part of a Section 92 application.

General

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

A summary of Board directives and undertakings from previous proceeding are summarized in Exhibit A.18.1.

A small number of intervenors, particularly VECC, have suggested that Hydro One has not complied with a number of previous Board directives and prior undertakings. Hydro One submits that it has appropriately responded to all previous Board directives and undertakings.

VECC has levied criticisms at the Applicant and its proposal to maintain the status quo of charging $1 per mwh for the Export Transmission Service ("ETS") tariff. VECC alleges that Hydro One has breached the settlement agreement which was reached in the Applicant's previous transmission rates case [EB-2006-0501]. Hydro One is troubled by this allegation.

Following the settlement conference in the EB-2006-0501 proceeding, Hydro One filed a settlement proposal with the Board which they subsequently reworded to read:

> *"The parties have agreed that the status quo ETS Tariff of $1/MWh should be maintained until the 2010 transmission rate setting process. In supporting the settlement the parties are supportive of the IESO undertaking a study of an appropriate ETS Tariff to be completed prior to the 2010 transmission rate re-setting process and through negotiation with neighbouring jurisdictions pursue acceptable reciprocal arrangements with the intention to eliminate all ETS Tariffs. It is understood that any change to the ETS tariff must be approved by the OEB as part of a rate setting process which Hydro One will initiate as part of the 2010 transmission rate re-setting process."*

Since the settlement agreement was approved in April 2007, the IESO has begun the process of examining appropriate ETS tariffs and possible changes to the reciprocal agreements. The IESO remains committed to providing its report and recommendations to the Board and stakeholders by June 1, 2009. The IESO has, in its latest update on the study of January 26, 2009 (available at www.ieso.ca/imoweb/consult/active_consultations.asp), indicated that should the Board consider new contracts (including possible elimination of the tariff) appropriate, it would then enter into formal negotiations. The timing of those negotiations and resulting contracts remains uncertain.

Hydro One filed this Application in the fall of 2008. Thus, it was unable to forecast its revenue requirement and external revenues on any basis other than the status quo. Hydro One remains committed to having a new ETS tariff approved by the Board at the appropriate time, and once the IESO has completed its work on the study.

Load Forecast and Revenue Forecast

2.1. Is the load forecast and methodology appropriate and have the impacts of Conservation and Demand Management initiatives been suitably reflected?

Hydro One is pleased to note broad support for its load forecast by Board staff and most intervenors. While VECC urged further review of certain aspects of the load forecast, VECC nonetheless argued that Hydro One's load forecast should be accepted for rate setting purposes in this Application.

Only AMPCO argued that the load forecasting methodology was inappropriate.

The load forecasting methodology used by Hydro One in this Application is the same methodology that was reviewed and approved by the Board in Hydro One's last Transmission Application (EB-2006-0501), with one minor modification. As a result of the increased volatility in system peak in recent years, Hydro One has reflected the relationship in energy and peak by adjusting the load so that the peak grows faster than energy over the forecast period. This adjustment was explained by Mr. But during the oral hearing [Tr. Vol. 5, pgs. 25-26]. The adjustment captures the evolving trends related to weather, changes in industrial processes and CDM actions from customers. This has resulted in a higher forecast of system peak, and consequently lower rates, than would otherwise be the case.

Hydro One does not believe that any further review of its weather normalization methodology is required. In response to direction from the Board in EB-2006-0501, Hydro One undertook a detailed weather normalization study which surveyed more than 50 utilities in North America [A.14.3, Attach. A]. Hydro One submits that the results of this study support the continued use of Hydro One's current weather normalization methodology. Hydro One's forecasts show little variability relative to actual weather corrected results [A.14.3, pgs. 23-24]. Most intervenors support Hydro One's load forecasting methodology and all intervenors submit that Hydro One's load forecast should be accepted for rate setting purposes.

As noted above, VECC levied some criticism regarding Hydro One's reflection of CDM in the load forecast. Hydro One submits that it followed the Board's direction from EB-2006-0501 in reducing peak load by 1,000 MW to account for CDM impacts in 2007 and has used the OPA's CDM forecasts for 2008 to 2010 that appropriately include demand response program expectations.

2.2 Are Other Revenue (including export revenue) forecasts appropriate?

A number of intervenors have argued that Hydro One's forecast 2009 and 2010 external revenues are too low. They have issues with three areas in particular (i) Secondary Land Use, (ii) Station Maintenance and Engineering and Construction Revenues and (iii) Export Revenues.

Secondary Land Use

Intervenors expressed concern that the test year forecast for Secondary Land Use is not in line with historic norms and should be rejected. Mr. Van Dusen explained during the oral portion of the hearing that one-time events have inflated the 2006 through 2008 revenues and that the test year forecasts are more in line with 2005 levels. For example, in 2008 the receipt of easement payments from the City of Toronto [Tr. Vol. 4, pg. 29] resulted in an anomalous increase in these revenues for 2008. Hydro One submits that it would be inappropriate to include unknown one-time events into the forecast, as suggested by intervenors, as there is no available information that would allow Hydro One to prudently forecast these events.

Station Maintenance and Engineering and Construction

A number of intervenors have also suggested that the Station Maintenance and Engineering and Construction revenues are too low as compared to historic averages. Hydro One’s evidence is that as a result of the increase in core work programs, minimal external work will be undertaken in the test years. Hydro One has repeatedly emphasized the growth in work programs in the test years. Demands will be placed on Hydro One’s work force to complete the additional planned work [E1.1.2, pg. 4]. As a result, Hydro One has made a decision to divert resources away from external work and has reduced the forecast for these revenues. Hydro One thus requests the Board accept its forecast for these revenues as submitted.

Export Revenues

Intervenors and Board staff argue that historical results should be the basis for determining export revenues in the test years. Board staff did recognize the fact that export revenues for 2008 were unusually high and may be anomalous. This anomaly is discussed on page 25 of the IESO 2009-2011 Business Plan which states that the exceptionally high exports experienced in 2008 “were directly attributable to pricing seams issues between New York ISO and neighbouring jurisdictions. These pricing seams issues encouraged marketers to schedule transactions through Ontario, resulting in simultaneous energy imports and exports for the IESO market.”

As noted in its pre-filed evidence Hydro One uses the forecast of exports in IESO business plans as the basis for estimating Export Revenues [H1.5.1, pg. 2]. On page 25 of the 2009-2011 Business Plan filed by the IESO [EB-2008-0340, B1.1.1], the IESO now forecasts the level of export to be 6.7 TWh in 2009 and 7.3 TWh in 2010. At the current export tariff of $1/MWh, this would result in Export Revenues of $6.7 million for 2009 and $7.2 million in 2010, which are well below the $12 million forecast by Hydro One in its Application.

Despite this downward revision in export volumes, Hydro One's position has not changed. $12 million is the requested amount for export revenues in 2009 and 2010, and Hydro One is prepared to absorb any forecast error related to export revenues.

CME states that Hydro One agrees that a variance account be established for export revenues. However, as clarified by Mr. Cowan, the variance account is proposed only in response to the IESO study being undertaken [Tr. Vol. 5, pg. 53]. It is not being proposed to record the differences between actual and forecast export revenues. The workings of such an account were confirmed by Mr. Innis in discussion with Mr. Buonaguro [Tr. Vol. 4. pg. 27].

Operations, Maintenance and Administration

3.1. Are the proposed spending levels for Sustaining and Development OM&A in 2009 and 2010 appropriate, including consideration of factors such as system reliability and asset condition?

As noted at the outset of this reply, a number of intervenors have argued for blanket reductions in proposed spending based on simple dollar or percentage comparisons. This theme runs rampant through the intervenor arguments on sustaining and development OM&A costs. What is notably absent is any compelling or persuasive challenge to the evidence regarding the reasons for the proposed spending. Hydro One submits, as it has in previous proceedings, that it is not enough to argue that overall costs have increased in percentage terms. The task of the regulator is to determine why costs have increased and then to make an informed judgment as to whether the increases are appropriate based on the evidence before it.

Several intervenors have used inflammatory adjectives like “astounding” or “staggering” to describe the proposed increases in test year spending. There have been suggestions that the Board should look to “historical norms”, Ontario CPI rates, or an arbitrary 3% baseline growth rate as the basis for determining what intervenors argue is a more appropriate increase in overall OM&A spending. Hydro One urges the Board to reject these arguments.

The proposed increases are primarily attributable to spending on very specific programs as explained in the evidence. Over the two test years, 60% of the increase in OM&A is attributable to spending to maintain Hydro One’s Station assets. While some components of the Stations program are decreasing over the test years, spending on Power Equipment and Ancillary Systems maintenance are the largest contributors to the increases.

The importance of the Power Equipment program and the scope of both planned and unplanned work that make up the maintenance spending for this program is detailed in the pre-filed evidence [C1.2.2]. The specific elements that make up the Power Equipment program are further detailed in Interrogatory I.4.10 and the increased work accomplishments associated with the planned work program are described in Interrogatory I.6.28 part b for transformers and part c for breakers. Similarly, a description of the extensive information gathered in evaluating the needs for this program is in Exhibit C1.2.2 and specific details on the reliability and condition assessment data driving the increased maintenance on power transformers, breakers and switchgear is explained in Interrogatory I.1.30.

The significant gap in reliability performance between Hydro One and other Canadian Electrical Association ("CEA") utilities, as measured by the frequency of forced outages on breakers and transformers, is clear [K3.1. Attach. B]. Of particular concern are the outage frequency and duration associated with 500 kV transformers which show an increasing gap in reliability performance relative to CEA levels. These gaps are one of the drivers of the increase in mid-life transformer refurbishments covered by this program which are planned to increase to 14 refurbishments over the test years in comparison to no refurbishments in either 2005 or 2006.

Another area of proposed increases is spending on ancillary systems, the need for which is detailed in Exhibit C1.2.2. Hydro One explained in its response to Undertaking J2.3, the specifics of the increase in work accomplishments over the test years relative to 2008. Increases are required in the level of planned maintenance to test and inspect the aging fleet of ancillary equipment. Grounding studies at select stations have identified a number of major issues. As a result, the number of stations being evaluated is increasing in the test years, as are the necessary repairs to address the findings from those studies.

Some intervenors expressed concern about the proposed increase in Development OM&A spending. Hydro One acknowledges that the spending associated with Research and Development (R&D) work is increasing by a relatively large degree. The key emerging issues and utility challenges driving the requirement for increased R&D spending were detailed in response to Interrogatory I.1.27. Details of the specific R&D projects planned for 2009, as well as the specific areas where projects and initiatives are being considered for 2010, have been explained in Interrogatory I.4.14. Hydro One is pleased to note that Board staff appear to accept the cost drivers as no specific concerns were raised.

Many intervenors have argued that the asset age demographics do not appear to support increasing maintenance needs for transformers and breakers. Reductions are thus urged.

Pollution Probe's analysis, based on the demographic data provided by Hydro One, shows that the number of transformers in the mid-life region over the test years is smaller than historical levels. This leads Pollution Probe to question why the number of refurbishments is increasing. Similarly SEC's analysis indicates that the number of units in the end-of-life region in 2010 is only 8% higher than 2008 for circuit breakers and 21% higher for power transformers. While these observations are correct, Hydro One's evidence demonstrates, as reiterated many times during the oral hearing, that asset age is only one indicator of general trends in spending. Investment decisions are made based on the actual asset condition (which includes a consideration of its age) and performance. As Mr. Currie stated during his testimony [Tr. Vol. 2, pg. 162]:

> "The mid-life and the end-of-life regions are more an indication of long-term trends that we're seeing. Those are the areas where we are anticipating that more work has to be done, but it's not the same as specifically selecting an asset for mid-life refurbishment. If it's in the mid-life region, it is a candidate, but we would select it on specific test requirements and expectations that we could preserve its asset life."

To highlight Mr. Currie's testimony in practice, the written evidence shows that no transformers were refurbished in 2005 and 2006, and only 1 unit was refurbished in 2007 even though there were more than 100 transformers in the mid-life region over that period. However, the deteriorating condition and performance of these assets now demands that work be undertaken to refurbish the most critical of these transformer assets. Accordingly, Hydro One planned for 4 transformer refurbishments in 2008 and an additional 14 over the two year test period. Hydro One submits this evidences shows it is prudent in refurbishing only those assets which show a demonstrated need for the work, and further evidences that spending decisions are not based on asset age alone. Hydro One submits the Board ought to consider its asset maintenance programs on all of the evidence, not simply asset age as appears to be urged by intervenors.

A great deal of time during the oral hearing was spent on what Hydro One internally refers to as a “minimum” spending level. As the Company’s witnesses noted, this was an unfortunate choice of term as it can be misleading. The potential to mislead is readily apparent as intervenors have seized upon the idea of the “minimum” and have urged the Board to make reductions to OM&A spending on that basis. Hydro One submits that it would be inappropriate to do so.

Hydro One explained, both in undertaking response J2.7 and during oral testimony by Mr. Van Dusen [Tr. Vol. 3, pg. 166-167], that the “minimum” level of investment is neither a sustainable level of investment nor is it in any way an acceptable target level of investment. The minimum levels of spending represent a level of investment which avoids unacceptable risk to meeting safety, regulatory or legal requirements over the planning horizon. As Mr. Van Dusen explained, spending at a “minimum” level may cover these statutory requirements in the short term, but it does not adequately address the deteriorating reliability and condition of Hydro One’s assets, which was also reinforced by Mr. Currie in his testimony [Tr. Vol.2, pg. 90].

It is also important to note that work programs and their associated spending requirement cannot be viewed in isolation from one another. They are interrelated as Mr. Currie explained [Tr. Vol. 2, pg. 184-185]:

> “And I think in the short term, when the investments are not made, we're going to see increases in corrective maintenance, which we have been seeing in the past, and that will show up in the OM&A side for the station sustainment. If we're not making end-of-life replacements and we're forcing assets to go beyond what we would like them to be, then we're going to see higher costs to maintain and keep them in the system at the desired reliability level. So it's not exactly a neutral thing, discretion capital. We will probably see increases in costs in OM&A that we won't have any discretion on, because things will happen and we will have to respond to them.”

If the intervenors’ suggestion to reduce spending to the “minimum” were accepted by the Board, the result would be a reduction in the proposed OM&A spending levels in the test years for power equipment and specifically reductions to the planned mid-life refurbishments and planned preventative maintenance program. It is probable that this would result in increased costs for the corrective maintenance component of OM&A spending and increased Sustaining capital needs in the future by contributing to the premature end of life of transformers and circuit breakers. As stated by Mr. Graham [Tr. Vol. 2, pg. 184], this deferred work could come at a higher cost.

SEC argues that Hydro One has not clearly demonstrated that the performance of the transmission assets is deteriorating based on some of the written evidence and from stakeholder presentations. Hydro One has never asserted that all of its assets show deteriorating performance trends. The data that the company presented as part of an initial stakeholdering session were not intended to provide a comprehensive picture of the state of the transmission assets. In fact, Hydro One witnesses testified to the fact that redundancy built into the transmission system may result in adequate performance of customer interruption metrics but may in fact be masking deteriorating performance at an equipment level [Tr. Vol. 2, pg. 103 and 234].

If the evidence on which SEC’s assertion is based is closely examined, it can be seen that the evidence does show some deterioration of year-over-year frequency and unavailability (duration) performance metrics. This is even more evident by review of the longer term performance trends from the data provided in Attachment B to Exhibit K3.1. The data in K3.1 demonstrates that the outage frequency trend lines for all transformers is negative, particularly for the 500 kV class of transformers. This evidence also shows a deteriorating trend for the unavailability (outage duration) performance of 230kV and 500 kV breakers, as well as 115 kV and 500 kV transformers. The performance trend for frequency of interruptions on all of Hydro One's breaker and transformer assets are also significantly worse than the CEA average. This is unacceptable to Hydro One. The company submits that this performance trend should also be unacceptable to Board.

The deteriorating reliability and asset condition for certain breakers and transformer asset classes accounts for the need to spend well above the minimum level for Power Equipment OM&A, as elaborated on in the response to Undertaking J4.2.

3.2. Are the proposed spending levels for Shared Services and Other O&M in 2009 and 2010 appropriate?

A number of intervenors criticized certain discrete areas of shared services and other OM&A. Hydro One will briefly address each of these criticisms.

VECC questioned Hydro One's capitalization of General Counsel costs and whether a provision for capitalization should be made for the test years. Infrequently, in the past, there has been specific capital projects identified where an increased or extraordinary level of legal involvement would be required. In these rare instances, the associated costs would be removed from the OM&A budget and charged to a capital project budget (for example the Bruce to Milton project in 2008). For the 2009 and 2010 test years, no capital projects have been identified that require a high level of activity from the General Counsel department. Hydro One has therefore not included a provision to capitalize additional General Counsel costs in the test years.

VECC also questioned the reasonableness of including International Financial Reporting Standards ("IFRS") implementation costs in revenue requirement since the requirements of IFRS are yet to be determined. Hydro One has included costs related to IFRS in the test period in preparation for meeting external reporting IFRS requirements. As a publicly accountable enterprise, Hydro One will be required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning January 1, 2011, with comparative figures reported for 2010. As such, IFRS conversion is required for closing balances effective December 31, 2009. As a reporting issuer, Hydro One also has ongoing disclosure obligations relating to its changeover to IFRS which commenced with the 2008 quarterly and year end Management's Discussion and Analysis. The costs to implement IFRS reporting at Hydro One are required and thus, in Hydro One's submission, prudent.

VECC and CCC have questioned the allocation of OM&A costs between Transmission and Distribution. In the pre-filed evidence, Hydro One included [C1.5.1, Attach. 1] Black and Veatch's ("B&V") "Review of the Implementation of Common Corporate Costs Methodology – 2008." Hydro One uses the B&V ("Rudden") study to determine the allocation of costs between its businesses. This methodology has been accepted in previous transmission and distribution Board Decisions. B&V concluded, in section E of this report, that "based on our review, Black & Veatch believes that the OEB-accepted methodology was applied by Hydro One to its Business Plan 2009-2013 data for its 2009 and 2010 Transmission Rates filing and the results, which are shown in Table 2, reflect a cost-based distribution of costs of providing the CCFS". Therefore the appropriate drivers have been used to allocate costs to transmission and distribution.

CCC submitted that most of the Corporate Communications budget should be allocated to Distribution, since the evidence referred to CDM and Smart Meter programs. The pre-filed evidence shows that the majority of tasks and responsibilities of the Corporate Communications department relates to both Transmission and Distribution operations. For example, Corporate Communications assists with Environmental Assessment studies and First Nation Relations, functions which are critical to the preparation and approval of Section 92 transmission applications. Hydro One thus submits that the Corporate Communication costs are supported by appropriate cost drivers and are properly allocated.

3.3. Are the compensation levels proposed for 2009 and 2010 appropriate?

Hydro One's position is that its 2009 and 2010 compensation levels are appropriate and are balanced by independently benchmarked productivity levels which are better than market median.

Over the past number of years, Hydro One has made steady progress in reducing overall per capita compensation in real terms and achieving further gains in the efficient utilization of the labour resources employed (i.e. getting more work done for each paid hour). Indeed, over the 2004 to 2010 period, Hydro One's average wage per person will only have increased by 5.7% in total or an average of 0.9% per year, far below the rate of inflation as shown in the following table. Between 2006 and 2010, wages per person will have increased by 1.2% in total over this period, or an average of 0.3% per year, far below Ontario economy general inflation and wage escalation. In the coming years, as new staff at lower wage scales and less provident benefit levels replace retiring Society and MCP employees, overall compensation will be further reduced.

Compensation Benchmarking and Levels

As directed by the Board in EB-2006-0501 Decision With Reasons, Hydro One engaged an independent party, Mercer/Oliver Wyman, to submit an independent, testable and repeatable report on compensation cost and productivity for Hydro One and comparable companies. The compensation benchmarking study found that the MCP and Society represented staff were 1% below and 5% above from market median respectively, or essentially at market median, whereas PWU represented staff were 21% above market median. As a result, Hydro One in total was 17% above market median.

In argument, SEC asserts that "by 2010, total compensation for PWU will be 27% higher than in 2004". SEC's alleged 27% increase is not supported by the evidence; PWU contract settlements over this period will have resulted in PWU wage schedules increasing by approximately 20% between 2004 and 2010. However, these percentage increases do not portray the whole picture. SEC and others totally disregard the efforts and gains that Hydro One has made by applying its staffing strategy over this period of time.

As summarized in the table[1] which follows, the evidence demonstrates that average PWU wages per employee will have increased by 0.6% between 2004 and 2010, or an average of 0.1% per year. Between 2006 and 2010, average PWU wages per employee will have decreased by 4.5%, or decreased by an average of 1.1% per year.

Hydro One submits that the evidence shows that it has successfully implemented its strategy to utilize lower paid and lower skilled staff to get substantially more work done at lower overall cost through this period. This has been achieved through: increased utilization of lower skilled hiring hall staff at lower compensation levels to contend with increased work volumes; the hiring of new junior Society staff at lower initial salaries as well as overall salaries; the hiring of new trades and other PWU staff at substantially lower initial wages as they start their apprenticeship programs; and more efficient utilization of staff to increase "wrench time" (this includes utilization of hiring hall staff to do the work when it is there during peak periods).

[1] Based upon Hydro One Networks Inc. year-end headcount payroll for transmission and distribution [C1.3.7, pg. 10, Table 3]

NETWORKS (Transmission & Distribution) TOTAL STAFF & WAGES

REPRESENTATION	TOTAL NO. EMPLOYEES	TOTAL WAGES ($)	WAGES ($) per EMPLOYEE	2004/2010		2006/2010	
				% CHANGE	AVERAGE % CHANGE/YR	% CHANGE	AVERAGE % CHANGE/YR
2004							
Building trades	571	36,164,442	63,335				
MCP	287	36,904,235	128,586				
PWU	3,080	246,066,961	79,892				
SOCIETY	935	85,096,183	91,012				
Total	**4873**	**404,231,822**	**82,953**				
2006							
Building trades	598	39,153,993	65,475				
MCP	476	59,707,957	125,437				
PWU	3,495	294,019,129	84,126				
SOCIETY	732	66,443,825	90,770				
Total	**5301**	**459,324,903**	**86,649**				
2010							
Building trades	960	72,028,390	75,030	18.5%	3.1%	14.6%	3.6%
MCP	630	90,411,804	143,511	11.6%	1.9%	14.4%	3.6%
PWU	4310	346,278,642	80,343	0.6%	0.1%	-4.5%	-1.1%
SOCIETY	1172	111,181,164	94,864	4.2%	0.7%	4.5%	1.1%
TOTAL	**7072**	**619,900,000**	**87,656**	5.7%	0.9%	1.2%	0.3%

Note: 2005 data was not used for comparative purposes due to the impact of the Society strike on compensation paid.

Sources (Total # employees & Total Wages):
2004 Data EB-2007-0681 Exhibit H-12-20
2006 & 2010 Data EB-2008-0272 Exhibit I-6-37

Hydro One has been successfully working with represented staff to achieve gains in workforce efficiency and productivity, effectively getting more work done for the same paid labour hour. This has included the PWU agreement to provide Management with the flexibility to direct and utilize the workforce, which has resulted in substantially increased use of lower paid hiring hall staff to do lower skilled work as and when required and the creation of new lower paid, lower skilled positions [C1.3.2, pg. 4].

In the case of Society represented staff, through negotiations, incentives and performance pay have been eliminated, new hires since April 2005 have 25% less provident pension plans, and since April of 2008 new hires are on substantially lower salary schedules [C1.3.2, pg. 9, Table 2]. In the case of new MCP staff, since 2004 they have been hired with less lucrative pension and benefits plan [C1.3.2, pg. 9]. As a result, as current staff leave the over all compensation cost will be reduced as new hires are brought in at lower compensation levels.

Due to the acute staff demographics issue in the electric utility industry, where up to half of current staff will be eligible to retire within five years, a substantial number of new hires were made in order to have fully trained replacement staff in place during the waves of retirements over the next decade. To find and hire new staff to keep on top of the high work demands are the market pressures that Hydro One and other electric utilities are facing today. It would be imprudent of Hydro One to follow the arbitrary suggestions of intervenors to not do the work that needs to be done and not employ and utilize the people that are needed to do this work.

Intervenors and Board staff suggest if Hydro One were privately held, its compensation costs would be lower. Hydro One has provided evidence that demonstrates that the Company has in fact been more successful than a privately held company in containing maximum wage rates for four “like” PWU positions. In Interrogatory I.1.41, Hydro One provided data which shows that for two highly skilled trades positions and two clerical positions, maximum wages paid by Bruce Power are 32% and 9% respectively higher than like positions in Hydro One; this does not take into account the assorted incentives and premiums Bruce Power pays its staff and which Hydro One does not offer.

Hydro One submits that it has controlled its compensation costs, despite the challenges it faces as a company where the overwhelmingly majority of its employees are unionized. Hydro One has acknowledged the Board’s concerns and responded to them. The evidence, when properly viewed, supports Hydro One’s position.

Productivity Benchmarking Results

As noted above, in response to the Board’s direction from previous proceeding, an independent party was retained to conduct a productivity benchmarking study. Hydro One held a number of stakeholder sessions so interested parties could provide input into the study, including the comparators, metrics to be used etc. Stakeholders participated actively in these sessions and informed the design of the study.

Having done so, the study is now criticized by a number of intervenors. Intervenors have expressed concerns with the relevance of the metrics used and the interpretation of the results. The conclusion from the compensation productivity study, outlined below, was heavily criticized: [A.16.2, Attach.1, pg. 2]

> "***All (Hydro One Transmission and Distribution productivity) indicators measured ranked better than median (i.e., more productive) except one, which is slightly below median (i.e., less productive).*** Hydro One Customer Service productivity indicators ranked the best among the peer group for all indicators examined. Examining the mix of indicators leads to the conclusion that Hydro One requires less workforce compensation to generate various units of output."

Hydro One, while cognizant of the limitations of the study, accepts the conclusions reached by Oliver Wyman. Hydro One submits that these high-level comparison results are substantiated by evidence and support Hydro One's position that:

> "the positive Hydro One productivity results balance Hydro One's total compensation being above the market median. The benchmarking study results provide further support for Hydro One's position that its continued productivity accomplishments offset its relative compensation levels." [A.16.2 pg. 3]

During the oral hearing, the metrics used in the study were criticized further. Thus, Hydro One asked Oliver Wyman to provide clear explanations of the productivity indicator definitions and calculations used in the study, along with an explanation of the standard practice in benchmarking studies for the definition of the median value [J4.3].

Despite the clarification provided by Oliver Wyman, intervenors' criticisms about the design and results of the study continue.

Energy Probe challenged the metrics used such as total compensation per MWh sold and total compensation per service territory.

For example, Energy Probe characterized the "per MWh sold" metric as "the total number of MWh sold through the transmission network". This is incorrect. As explained by the author, the study looked at the sum of both transmission and distribution MWh sold by the company [J4.3, Attach. 1]. Thus, if a comparator company has a larger proportion of the distribution system within the transmission service territory it serves as compared to Hydro One, then its "MWh sold" will include proportionally more distribution "MWh sold".

The productivity measure relating to total compensation per service territory was also criticized during the oral hearing. Oliver Wyman clarified that [J4.3]:

> "Service territory was provided to us in our survey as the area (sq. km) over which service is provided to customers. Where possible we checked the calculations for appropriateness. When both a distribution and transmission service territory were provided, we used the "union" of those measures so that overlapping territory was not double counted. The service territory area that was provided [for Hydro One] represents only 60% of Ontario's total area. For companies that have more distribution in their mix, they will have more distribution compensation costs, they will have more service territory to normalize this."

It appears that Energy Probe and other intervenors have completely disregarded this clarification. Hydro One acknowledges that one of the company's witnesses erred during testimony and mistakenly advised that the service territory was 96% of Ontario's total area. This prompted Hydro One to request the clarification above. Notwithstanding, the appropriate data and the clarifying information has been ignored. Hydro One thus asks the Board to view with caution intervenor arguments in this area, as well as comments such as "LDC territory gets included in Hydro One's service territory using this definition", which are simply incorrect.

There was further confusion during the hearing about the presentation of data obtained from the study and the mean and median value utilized. On the surface, Hydro One felt this required clarification which was sought from Oliver Wyman. In response, Oliver Wyman clarified that "the median value is the median value of the comparison set excluding Hydro One. Hydro One is then compared against that comparison set. This is a standard practice in benchmarking studies."

In addition to the evidence provided via the productivity benchmarking study, Hydro One notes that its productivity compared to other Ontario utilities as reported by this Board and its external experts PEG, establishes that Hydro One's Distribution business is at median in terms of establishment of (productivity) stretch factor assignments for the OEB's 3rd Generation Incentive Regulation for LDC's (EB-2007-0673 "Addendum to the Supplementary Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors", January 28, 2009) and efficiency ranking ("Sensitivity Analysis on Efficiency Ranking and Cohorts For the 2009 Rate Year: Update" by PEG, December 3, 2008).

3.4. Is Hydro One Networks' proposed transmission overhead capitalization rate appropriate?

Hydro One notes that intervenors and Board Staff did not challenge Hydro One's proposed transmission overhead capitalization rate.

3.5 Are the amounts proposed to be included in the 2009 and 2010 revenue requirements for income and other taxes appropriate?

Hydro One's methodology for the calculation of income and capital tax was not challenged by intervenors, except for two areas: Apprenticeship Tax Credit and Scientific Research and Experimental Development Tax Credit ("SR&ED") and CCA for Computers. In addition, some challenges were made to the proposed property taxes. Hydro One will address each of these areas.

Apprentice and SR&ED Tax Credits

BOMA/LPMA, with support from CME, questioned whether Hydro One included the reduction associated with the Apprentice and SR&ED tax credit in its Calculation of Utility Income Tax filed at Exhibit C2.6.1, Attach. 1.

Hydro One has included the estimated Apprenticeship and SR&ED tax credits in its calculation of utility income taxes on lines 12, 13 and 20 of the referenced exhibit for the transmission business. The tax credits were allocated to Transmission and Distribution based on historical experience. In determining the Transmission benefit for SR&ED for 2009 and 2010, the known R&D expenditures were used.

CCA – Computers

BOMA/LPMA, CME and VECC requested that the change in CCA rate for Class 50 assets introduced as part of the January 2009 Federal Budget be implemented now by reducing that taxable income, rather than captured through the applicable deferral account. Hydro One agrees with BOMA/LPMA's calculation and is prepared to decrease the regulatory income tax computed in Exhibit C2.6.1, Attach. 1.

Property Taxes

BOMA/LPMA and VECC have argued that the forecast property taxes in 2009 be reduced by $3.7 million and by $3.9 million in 2010, based upon 2008 actual Property and Other Taxes.

The projected property tax costs in 2009 and 2010 are based on anticipated property tax expenses that take into consideration a number of variables. The Company projected increases in property taxes of 4%. This 4% increase is premised upon an anticipated 2% increase in the assessed value of Hydro One properties, and a forecast 2% municipal tax increase for years 2009 and 2010 [I.2.15, I.4.22].

Hydro One is experiencing higher assessed values due to reassessments from the Municipal Property Assessment Corporation ("MPAC"), post 2008. At the same time, Hydro One expects municipal tax rates to increase across the province. These increases have already materialized in a number of municipalities, including the GTA which show a trend higher than the 2% projected tax increase filed. For example, the City of Toronto recently approved its budget for 2009 which includes a 4% increase in municipal property tax.

Hydro One expects diminishing opportunities for tax refunds in the future given the scrutiny applied by MPAC to Hydro One properties. Several municipalities have indicated to Hydro One their plans to initiate assessment appeals, challenging the tax assessments on Hydro One's properties. If successful, higher property tax expenses will result.

As a result, Hydro One submits the Board should reject BOMA/LPMA and VECC's requests for reduced property taxes.

Other Tax Rate Changes

In preparing the rate order for the 2009 and 2010 test years Hydro One will reflect the impact of the reductions in the statutory tax rates from the March 26, 2009 Ontario Budget as noted by Mr. Cowan [Tr. Vol. 5, pg. 40]. Any other tax-related impacts will be reflected in the deferral account for future review and disposition.

3.6 Is Hydro One Networks' proposed depreciation expense for 2009 and 2010 appropriate?

Hydro One notes neither Board staff nor the intervenors raised any concerns with Hydro One's test year depreciation forecast subject to the Board's Decision regarding capital expenditure levels.

Capital Expenditures and Rate Base

4.1. Are the proposed 2009 and 2010 Sustaining and Development and Operations capital expenditures appropriate, including consideration of factors such as system reliability and asset condition?

Board staff and most intervenors have highlighted that Hydro One did not achieve its approved capital investment levels in 2007 and 2008. Hydro One has openly acknowledged this fact. Cognizant that this would be of concern to the Board and intervenors, Hydro One provided extensive evidence of the factors contributing to the underachievement in capital spending levels in 2007 and 2008 [D1.1.2, I.6.47, Tr. Vol.1 pg.64].

Hydro One urges the Board to reject this concern with 2007 and 2008 accomplishments as a basis upon which to justify reductions in the proposed 2009 and 2010 capital program. As stated by Mr. Graham, the steps Hydro One has taken, and continues to take, will ensure it can deliver on its proposed capital plans as it did in the second half of 2008 [Tr. Vol.1, pg. 53-54].

Hydro One's Exhibit A.14.7 outlined the actions being taken in seven specific areas that will contribute to the Company's ability to complete the test year Capital program. Contrary to the submission of Board staff, some of these actions do represent new methods as evidenced by Hydro One's development of new standardized designs for "PCT in a Box" [A.14.7 pg. 7, Tr. Vol. 2 pg. 96], the development of long lead material tracking system [A.14.7 pg. 7, Tr. Vol. 1 pg. 54], and leveraging of the newly installed Cornerstone systems to better plan and schedule its work [A.14.7 pg. 9, Tr. Vol.1 pg. 189]. More significantly, Hydro One believes it is not necessary to implement "radically different techniques", as Board staff suggest, in order to significantly increase its ability to complete a larger planned work program. Contracting out work is an excellent example of this.

Hydro One has historically contracted out some work. However, as Mr. Sauter testified, in 2009 Hydro One has over $300 million of turnkey contracts, which is about 53% of the Development capital program for 2009 and is $200 million more than what it was in 2008 [Tr. Vol. 1, pg. 54]. Mr. Sauter further stated that the amount of turnkey work will increase to approximately 70% of the Development capital in 2010 [Tr. Vol. 1, pg. 66]. As shown in the table below, when the volume of work to be done by turnkey contracts is taken out of the capital spending program, the remaining capital work to be completed in 2009 and 2010, on average, represents a level demonstrably achieved in 2008.

Capital Expenditures

($M)	**2008**	**2009**	**2010**
Total Sustaining (S) Capital *	280	280	322
Total Development (D) Capital *	311	553	659
Total S & D Capital	591	833	981
Less Turnkey Contract Work	100	300	460**
Remaining S&D Capital	491	533	461

* per D1.3.1, Table 1

** Based on 70% of 2010 Development Capital of $659 million [Tr. Vol. 2, pg. 66]

Board staff erroneously suggests that approval of the proposed capital program may result in “over-collection from the ratepayers in the short term” and claim that “in 2007 there was an over-collection of 21% in the year, and in 2008 there was over collection of

9% in the year". BOMA/LPMA also erroneously suggest that Hydro One collected a return on capital expenditures that it planned, but did not make, in 2007 and 2008. These assertions are simply incorrect. Capital expenditures have been confused with in-service additions. As shown in Exhibit D1.1.2, the total in-service additions for 2007 were essentially on plan resulting in no "over collection" from ratepayers.

The same considerations apply for the 2009 and 2010 Capital program. It is worth noting that about $711 million, or 52% of the $1,369 million in gross Development capital spending over the two test years, is not scheduled to be placed in-service until after the test years [D1.3.3, Tables 2, 3, 4 and 5, I.1.75]. Therefore, even if Hydro One does not complete all of the planned capital work, to the extent that capital work not completed is associated with programs only scheduled to come in-service beyond the test years, there will be no impact on the requested rate base, and consequently no impact on revenue requirement.

CCC argued that Hydro One under spent capital in 2007 and 2008 and "the world did not end". While true, the written and oral evidence demonstrates there are consequences associated with this under spending [D1.3.1, pg. 6, Tr. Vol 2, pg. 184]. Reduced capital spending can also contribute to higher OM&A costs as discussed for Ancillary maintenance under issue 3.1 above.

The Sustaining Capital program proposed for 2009 is $279.9 million, which is almost identical to the actual Sustaining Capital spending of $280.4 million in 2008 [D1.3.1, pg.2, Table 1]. For 2010, Hydro One proposes a 15% increase over 2009 levels. The increase in Sustaining Capital is largely attributable to increased spending on Stations assets. The reasons for the increases are well documented in the pre-filed evidence [D1.3.2, pg. 5-46] and in numerous interrogatory [I.1.55, I.1.70, I.4.32, I.6.51, I.8.21-23] and undertaking responses [J2.3]. Hydro One notes that both VECC and EP are supportive of the planned Sustaining capital program and no intervenors raised concerns with any specific elements of the proposed Sustaining capital program.

It is the Development capital program that contributes most significantly to the proposed increase in spending over 2008 actual spending. However, not all areas of the Development program contribute to this increase. In fact, average net capital spending over the two test years drops relative to 2008 actuals for Area Supply Development and Generation Connection projects, and remains relatively flat for Load Customer Connection projects.

Inter Area Network Transfer Capability ("Network") projects detailed in Table 2 of Exhibit D1.3.3 contain substantial proposed increases over historical levels. However, reliance on only historical norms for Network projects completely ignores that this work consists of large, expensive, discrete projects that are largely driven by the changing generation patterns in the province, and which fall outside the area of historical norms associated with a largely stable transmission system. The Bruce to Milton project (D2) is a good example of this.

The Bruce to Milton project is a multi-year project previously approved by the Board in a Section 92 proceeding [EB-2007-0050]. This project alone contributes $170.3 million and $263.1 million in capital expenditures for 2009 and 2010 respectively and is certainly outside recent historical norms.

Hydro One is pleased to note support from AMPCO for the proposed Network Development Capital projects (D1-D14). Eleven of the fourteen Network projects are proceeding on the basis of direction received from the OPA. Hydro One has already received a formal OPA recommendation for 6 of those projects and anticipates receiving recommendations for the remaining 5 projects. As confirmed by Mr. Graham, Hydro One staff is in almost daily contact with OPA staff [Tr. Vol. 1, pg. 198] and based on this continuing interaction Hydro One believes it will receive the remaining OPA recommendations shortly [Tr. Vol. 1 pg. 24-25]. The Investment Summary Documents ("ISD") for these projects confirms that the proposed work will not proceed until a formal letter of recommendation is received from the OPA. Hydro One believes this satisfies

VECC's suggestion that the OPA provide clear and formal support for projects it would like Hydro One to undertake.

Hydro One notes that 3 of the 5 projects for which an OPA recommendation letter are pending relate to accommodating increased new renewable generation in Northern Ontario. The other 2 projects relate to incorporating additional generation at the Bruce complex and potential wind generation in the Georgian Bay area. The need for these projects is particularly salient with the announcement of the Green Energy Act, which appears likely to incent and/or expedite renewable generation across the province.

Some intervenors have argued that Hydro One should include detailed evidence from the OPA on the integrated generation and transmission projects as part of its pre-filed evidence. Hydro One disagrees with this proposition. Hydro One has provided a description of the need and scope of the work required for all capital projects for which it is seeking approval as part of the ISDs provided in Exhibit D2.2.3. Additional supporting information was also provided for several Network projects, including copies of the letters of recommendation for projects D2, D3, D4, D7, D8 and D12 [J1.3], details of the alternatives considered for projects D3 to D10 [J1.4] and IPSP related details for a number of projects [I.1.61, I.1.62, I.6.56].

It was also suggested that some of the Capital projects driven by customer load growth need to be revisited because load growth is decreasing as a result of the economic downturn. However, Local Area Supply ("LAS") projects proposed in Hydro One's application are to address local load growth, and as Mr. Graham stated in his testimony [Tr. Vol. 1, pg. 32-33],

> "in some cases we have overloaded facilities already, so we're just effectively catching up. In other cases we would be basing it on a forecast for, there's still growth expected, yes."

LAS project D22 (Supply to Essex County) will be subject to further approval under a Section 92, and therefore the need for this work will be fully tested in that forum. In any case, D22 is scheduled for in-service beyond the test years and does not impact rate base.

With respect to Load Customer Connection projects, Mr. Sabiston summarized in his testimony [Tr. Vol. 1, pg. 40-41] that thirteen of the fifteen projects are fully anticipated to materialize based on customer agreements or because they are required to address end-of-life replacements.

Some intervenors suggested there is a regulatory gap in the approvals associated with Network projects. As discussed at length in the exchange between Mr. Graham and Mr. Warren during the oral phase of the hearing [Tr. Vol. 2, pg. 8-19], Hydro One's role is to provide cost effective transmission solutions to the OPA for their consideration in evaluating the cost effectiveness of their various plans. Hydro One accepts the OPA's recommendation, if required, as justification for the need to proceed with the transmission component of the project in furtherance of the OPA's legislated mandates.

In their submissions, Board staff suggested that "Hydro One should file evidence in its next rate case which demonstrates a sound methodology for establishing an appropriate social discount rate". Hydro One does not believe that it should be identified as the entity responsible for leading evidence to establish an appropriate social discount rate. If Hydro One uses a social discount rate for the purpose of evaluating any Network capital projects in the future, the Company would use a rate consistent with what the OPA would be using at the time for evaluating projects of a similar nature.

Pollution Probe raised a concern about short circuit constraints in the Toronto area. Pollution Probe urged the Board to order that Hydro One develop and have ready a preliminary plan and budget to address the constraints within 6 months.

Hydro One is in the process of developing a plan for dealing with the short circuit issues in Toronto. Hydro One has reprioritized activities related to the planning and estimating of work at Hearn, Leaside and Manby to address the short circuit constraints, such that development plans are now scheduled to be completed by the end of 2009. Hydro One submits this is the earliest timeline in which this work can be achieved given the complexities that need to be dealt with. Hydro One submits its current plans, timing and scope of work largely address Pollution Probe’s concerns.

4.2. Are the proposed 2009 and 2010 levels of Shared Services and Other Capital expenditures appropriate?

CCC questions Hydro One’s proposed capital and OM&A expenditures on head office facilities, and claims that the head office costs are ‘imprudent in light of the economic conditions in the province” and should thus be deferred. Hydro One has addressed the impact of the current economic climate earlier in this Final Reply Argument and submits that this project must be assessed on the evidence provided, not on current economic conditions.

There has been an increase in Facilities and Real Estate (“F&RE”) expenditures over the test years. As explained in the prefiled evidence [C1.2.8, D1.3.8 and D2.2.3], these expenditures are driven by the expiry of Hydro One’s head office lease, the need to ergonomically accommodate a growing workforce, improvements to the heating/ventilation/air-conditioning systems and health and safety concerns as noted by Mr. Van Dusen [Tr. Vol 3, pg. 168]. As a result, Hydro One believes that this planned work must be completed in 2009 and 2010 and requests that the Board approve the proposals.

4.3. Are the amounts proposed for rate base in 2009 and 2010 appropriate?

Hydro One's forecast transmission rate base for 2009 is $7,034 million and $7,651 million for 2010. No party challenged the company's proposed rate base. Only VECC mentioned, in passing, that any reduction in capital expenditures made by the Board would impact resulting capital additions for 2009 and 2010. Hydro One has responded to intervenor and Board concerns in response to Issues 4.1 and 4.2 and will not repeat them here.

4.4. Is the forecast of long term debt for 2009-2010 appropriate?

Although this issue does not specifically deal with all components of Hydro One's Cost of Capital, some issues were raised during the oral hearing and in intervenor argument regarding the timing of cost rate updates and the appropriateness of Hydro One's deemed long-term debt. Hydro One will address the intervenors' concerns with these issues prior to addressing the long-term debt forecast for the test years. The draft rate order submitted to the Board will reflect the reduction in revenue requirement for the test years, reflecting the Board's final determination of the appropriate values for Return on Equity ("ROE") [I.1.10].

Cost of Capital Rate Parameter Update Timing

Hydro One has requested the Board update the Cost of Capital parameters for ROE, short-term debt costs and deemed long-term debt costs as documented in the Board's December 20, 2006 "Cost of Capital Report" [Appendix B, pg. 111]. Following this methodology, rates for 2009 would use the March 2009 Consensus Forecast and March Bank of Canada data. Rates for 2010 would use the September 2009 Consensus Forecast and Bank of Canada data for the month of September. Hydro One notes BOMA/LPMA supports this approach.

CME has requested the Board apply the rates issued on February 24, 2009 [J5.2] for the LDCs being rebased in 2009 for both 2009 and 2010 test years, rather than Hydro One's proposal. Hydro One submits CME's proposal is inappropriate and is contrary to the Board's own guidelines noted above.

Hydro One notes the Board has initiated a proceeding [RP-2009-0084] to review whether any modifications are needed to the Board's formulaic approach used to establish the parameters in their February 24, 2009 memo. Results of this proceeding could change the ROE and interest rate values for the LDCs rebasing in 2009. Given the uncertainty around an appropriate ROE for all utilities, Hydro One submits that its proposed approach is appropriate given the current economic circumstances.

Hydro One submits that the Board can either issue letters with the new cost of capital rates once the March and September 2009 data is available, as suggested by BOMA/LPMA, or Hydro One can reflect the March and September 2009 Consensus and Bank of Canada parameters in the subsequent rate orders. The draft rate order submitted to the Board will reflect the reduction in revenue requirement for the test years, reflecting the Board's final determination of the appropriate values for ROE, short-term debt costs, deemed long-term debt costs and forecast third party long-term debt.

Deemed Long-Term Debt

Intervenors have objected to including deemed long-term debt amounts of $206 million in 2009 and $0.3 million in 2010 in Hydro One's capital structure [B1.1.1, Table 1]. Intervenors claim this is inconsistent with the Board's "Cost of Capital Report".

Hydro One disagrees with the intervenors and requests that the Board reject the suggestion that deemed long-term debt should not be included in the capital structure of the Company. The Board approved a deemed long-term debt component in Hydro One's last transmission application of $125 million for 2007 and $66 million for the 2008 test year [EB-2006-0501] and an amount of $53 million for the 2008 test year in the last distribution decision [EB-2007-0681]. There has been no change in circumstances to suddenly exclude a deemed long-term debt component in Hydro One's capital structure to balance with rate base. Consistent with these two previous Board Decisions, the approved deemed long-term debt rate should be applied to the deemed long-term debt component in determining Hydro One's overall Cost of Capital and not at the average cost of actual and forecast third party long-term debt.

Cost of Third Party Long-Term Debt

Hydro One has not updated its forecast of long-term debt consistent with the Company's practice of not updating any forecast numbers for the test years. BOMA/LPMA and other intervenors agree with this approach for the test years but feel Hydro One should update its application to reflect actual debt issuances and cost rates for 2008. Hydro One submits that this is another example of selective updating requested by intervenors. Hydro One is concerned that intervenors urge the Board to ignore updates where there are known cost increases and instead focus only on areas of cost reduction. As with any forecast, there will be upsides and downsides. Hydro One thus requests that the Board accept the utility's balanced approach and reject arguments of selective updates.

Any cost decreases resulting from actual third party long-term debt issuances in 2008 which differ from those levels forecast for the bridge year, will be more than offset by issues in the test years at rates higher than forecast given the current economic situation. For example, as shown in Undertaking J3.1, if Hydro One were to update its cost of third party long-term debt to reflect the Board's January 24, 2009 letter, the average cost of third party long-term debt in 2009 would rise to 5.98% from 5.90% and to 5.88% from 5.80% in 2010. Hydro One was not asked to file the combined impact of actual 2008 issues and the adoption of the January 2009 Consensus outlook on the above rates. Such an analysis would show that the 2009 rate would rise from 5.90% to 5.92% and the 2010 rate would rise from 5.80% to 5.84%. As such the Board should accept Hydro One's cost of third party long-term debt as filed. Since debt costs will now be higher than filed, ratepayers will still benefit from the Board accepting the as-filed third party long-term debt costs for the test years.

Finally, BOMA/LPMA was not clear as to whether the $300 million shown in response to Interrogatory I.2.20 was mapped in total to Hydro One Transmission. Hydro One confirms that the full amount was mapped to Hydro One Transmission in the fourth quarter of 2008.

Treasury OM&A Costs

BOMA/LPMA, with agreement of CME, submitted that Treasury OM&A costs that are primarily wage costs should be reduced by $0.4 million in both 2009 and 2010. Hydro One submits that the increase to OM&A is due to higher staff levels, not just wage escalation. The borrowing program is expected to increase significantly from 2006 and 2007 levels, requiring more support to ensure cost effective liquidity and access to debt markets at all times. Hydro One asks that the Board reject any suggested reductions.

Deferral/Variance Accounts

5.1. Are the proposed amounts and disposition for each of the deferral and variance accounts appropriate?

Hydro One is requesting that the Board approve disposition of its Regulatory Assets up to June 30, 2009 over a four year period as outlined in the evidence [F1.1.1]. The proposed disposition period is consistent with recovery periods previously approved by the Board in Hydro One's last transmission proceeding [EB-2006-0501].

Several intervenors, including Board Staff, BOMA/LPMA, and VECC, have recommended the disposition period be reduced to 18 months, two years or three years. Hydro One is not opposed to an alternative disposition period. If the Board is inclined to do so, Hydro One suggests recovery over an 18 month period commencing July 1, 2009 to December 31, 2010. Hydro One believes that of the alternatives proposed, 18 months is the most appropriate as this coincides with the rate period for which approval is sought in this application.

BOMA/LPMA have requested clarification of two issues regarding the 2009 regulatory asset refund amount: (i) the reconciliation of the $(4.7) million regulatory asset refund shown in I.1.15 with the $(2.3) million shown in Exhibit F2.1.2 and (ii) if Hydro One has underestimated the 2009 Rates Revenue Requirement in Table 2 of Exhibit E1.1.1 by $4.4 million.

Hydro One is pleased to provide the requested clarification.

(i) Interrogatory I.1.15 shows the refund of regulatory assets in the amount of $(4.7) million This represents a 12 month period refund of the total regulatory asset of $(18.3) million amortized over 48 months. Exhibit F2.1.2 shows the

2009 refund of $(2.3) million. This amount represents the regulatory asset refund which has been included in the proposed 2009 rates, to be refunded to customers from July 1, 2009 to December 31, 2009.

(ii) The rates revenue requirement has not been underestimated. Exhibit E1.1.1, Table 2 illustrates the requested Rates Revenue Requirement for the period January 1, 2009 to December 31, 2009. Line 8 of the same table includes the $(4.4) million recovery of Market Ready Project and Export Credit Revenue refunded from January 1, 2009 – June 30, 2009 [J3.4] the remaining $(4.4) million to be refunded from July 1, 2009 – December 31, 2009, plus the $(6.1) million Other Regulatory Assets.

5.2 Is the proposed continuation of the deferral/variance accounts appropriate?

Hydro One submits that the continuation of the deferral/variance accounts is appropriate and was not challenged during the proceeding.

5.3 Are the proposed new Deferral/Variance Accounts appropriate?

Hydro One requests approval to establish three new deferral accounts for Transmission as follows:

- Pension Cost Differential;
- IPSP and Other Preliminary Planning Cost (“IPSP”); and
- Transmission System Code & Cost Responsibility Changes.

Hydro One is pleased to note that Board Staff and Intervenors do not oppose continuing the use of the Pension Cost Differential and the Transmission System Code & Cost Responsibility Changes accounts. Hydro One respectfully requests that these deferral accounts be approved as requested.

Hydro One also seeks the Board's approval to establish the IPSP and Other Preliminary Planning Costs deferral account to record costs associated with preliminary work required to advance 18 transmission-related projects required by the OPA in their IPSP and to incorporate Darlington "B" GS into the transmission system.

Board Staff argued that the account is justified, but asked that Hydro One address, based on the evidentiary record, how this account would meet the four Board criteria for the establishment of a deferral or variance account. Hydro One submits that the proposed account meets the Board's criteria as follows:

i. *Causation – the expense must be clearly outside of the base upon which rates were derived*. The expenses to be captured in this account have not been included in Hydro One's base revenue requirement [C1.2.3, Sec. 3.0 and F1.1.2, pg. 2). The account is required because of the proposed IPSP plan and due to a Government directive with respect to required work at Darlington GS.

ii. *Materiality – the costs must have a significant influence on the operation of the electricity distribution utility*. The total cost of the identified Development Work for IPSP and Other Long Term Projects is $47.9 million, with $19.2 million forecast to be spent in the test years [C1.2.3, Table 1]. Hydro One submits that both the overall costs and the amounts and the test year spending proposals are material to the operation of the utility.

iii. *Inability of Management Control – the cost must be attributable to some event outside of management's ability to control.* The projects associated with this account are not in Hydro One management's control. As a result, while Hydro One anticipates that these projects will come to fruition, and it must begin development work in order to meet anticipated in-service dates, at this time there is no assurance that capital assets will materialize as a result of the proposed expenditures.

iv. *Prudence – the expense must have been prudently incurred. This means that the option selected must represent the most cost-effective option (not necessarily least initial cost) for ratepayers.* The costs for which Hydro One is seeking approval and proposes to be captured in the deferral account consist of pre-engineering and planning work required to prepare project submissions for Environmental Assessment and Leave to Construct approvals. These costs are all subject to Hydro One's rigorous planning process. In addition, the need for these projects (and the associated costs) was identified by the OPA to meet the government's Supply Mix Directive. As explained in Exhibit F1.1.2 "Hydro One Transmission believes it is prudent to undertake this necessary preliminary work, prior to the approval of the IPSP in order to meet the required in-service dates."

Hydro One submits the requested account meets the Board's four criteria and thus respectfully requests that the Board approve establishment of the account.

A number of intervenors rejected the need for this account. AMPCO and SEC argued that the expenditures proposed to be captured in this account were capital expenditures and should be treated accordingly. This argument is incorrect. Accounting policies preclude this suggested treatment. Accounting policy only allows costs associated with the selected project preferred alternative to be capitalized. The projects that do not meet the capitalization criteria would be considered OM&A as noted by Mr. Innis [Tr. Vol. 4, pgs. 93-94]. Since Hydro One will not know at the time these costs are incurred if the project will or will not proceed, these costs would be treated as OM&A, not capital. The variance account will protect ratepayers from the immediate expensing of these costs.

In addition, AMPCO urged the Board to disallow the proposed account on the basis that Hydro One would gain a competitive advantage if the projects proceed and are tendered. Hydro One disagrees. Other entities are now at liberty, like Hydro One, to undertake pre-engineering work at this time. The proposed deferral account does not prevent other entities from doing so.

Hydro One thus submits that the new and continued accounts be approved as requested. Otherwise, Hydro One requests that the OM&A in the requested revenue requirement in 2009 be increased by $8.0 million and 2010 by $11.2 million, to reflect the expensing of the IPSP pre-development work in the period the expenditure is made.

In addition to the accounts that Hydro One has requested, many intervenor arguments included requests for deferral accounts, for Capital Expenditures, External Revenues and Export Service Revenue. Hydro One submits that the intervenors have not established the need for these accounts based on the four criteria for the establishment of a deferral account and the Board ought not establish any additional accounts, beyond those that have been requested by the Company.

Cost Allocation

6.1 Would it be appropriate to make change to cost allocation in response to the study submitted on line connection costs for customers directly connected to networks stations?

Board Staff recommends that the Board order Hydro One to undertake a detailed cost allocation study for the 45 Delivery Points that, under the alternative scenario evaluated in the study, would pay Line Connection charges and that Hydro One should communicate the results of the study to the affected customers.

Hydro One firmly believes that further study on this issue is not warranted. In their argument, VECC agrees that Hydro One has met the commitment made in the EB-2006-0501 Settlement Agreement and no changes need to be made to the methodology used to determine who pays line connection charges and how such charges are determined.

Hydro One's position is that the pre-filed evidence very clearly shows that the large range of impacts under the alternative scenario studied is not due to the change in cost allocation but rather the result of the change in charge determinants applied to the Delivery Points billing parameter [G1.3.1, Attach. 1, pg. 7-8]. Further study on this issue will only fine tune the magnitude of the cost allocation, but the charge determinants would not change. Therefore, further study would not be useful to the Board in addressing the key issue, which as discussed in Interrogatory I.6.65 is:

> "whether customers supplied at a Network Station should have to pay Line Connection".

The Ontario Uniform Transmission Rate Schedule currently specifies that "customer demand will not incur line connection service charges for demand at a transmission delivery point located at a Network Station". As Hydro One's study shows, there are minimal assets that could be attributed to connecting a customer delivery point located at a Network station [G1.3.1, Attach. 1, pg. 5, Table 1]. As such, it could be perceived as inconsistent with the principle of cost causality for such minimal use of allocated Line Connection assets to result in the levying of a Line Connection charge that recovers the total cost of all customers' Line Connection facilities.

6.2 Has Hydro One Networks' cost allocation methodology been applied appropriately?

There were no concerns raised by intervenors on this issue, other than VECC who commented that it is satisfied that Hydro One has applied the cost allocation methodology appropriately.

Charge Determinants

7.1. Is the proposal to continue with the status quo charge determinants for Network and Connection service appropriate?

AMPCO has submitted a proposal to change the Rate Design for Network charges and proposes that the Network charges be based on the 5 highest peak days in the prior year. In its Argument in Chief, Hydro One indicated that it did not at that time have a firm position on AMPCO's proposal. Hydro One required input from intervenors, with the caution that the rate impacts of the proposal may be larger than argued by AMPCO.

The AMPCO proposal is supported only by PP and conditionally by CME. The proposal was rejected by EDA and VECC. OEB Staff, BOMA & LPMA, CCC and SEC recommend that AMPCO's proposal should be further studied. This clearly illustrates the dilemma faced by Hydro One. There is no clear consensus amongst the various stakeholders that a change is required to the Network charge determinants. As a result, Hydro One's position remains that it does not propose to change the charge determinants in this proceeding. Hydro One submits that the Board, at this time, should reject AMPCO's proposal.

In EB-2006-0501 Hydro One evaluated an alternative to the current charge determinants for Network charges that was based on customer's coincident demand based on 12 peak months. AMPCO's current proposal is based on the 5 highest peak demand days. The evidence filed in EB-2006-0501 [H1.3.1, pg. 3] demonstrated that the impact was estimated to be a 2% increase in Network charges for LDCs and about a 15% decrease in Network charges to end-use transmission customers. Based on this analysis, Hydro One is concerned that the rate impacts from AMPCO's current proposal are likely to be even larger since the current proposal is based on the 5 highest peak days versus the 12 peak alternative previously evaluated. Hydro One notes that these baseline impacts result from simply changing the Network charge determinants methodology, and assume no load shifting by customers. The transmission cost increase to other customers of $899,206 claimed by AMPCO result from the load shifting driven by the change in methodology [I.17.14, pg. 9]. Hydro One believes AMPCO's claimed transmission cost impacts do not capture the baseline impacts resulting from simply changing the methodology.

Hydro One shares VECC's concerns with AMPCO's proposal and in particular VECC's concerns with respect to Dr. Sen's empirical analysis of the effect of changes in demand on HOEP and the low R-squared values for some of his equations. Of particular concern is AMPCO's determination of elasticity of demand with respect to electricity price based on an implicit assumption that on-peak and off-peak prices are independent so that it is possible to change one while controlling for the other one [AMPCO evidence pg. 6-11]. Hydro One does not believe this to be appropriate.

Hydro One is also concerned with the low r-squared value for the pricing equation which Dr. Sen testified "has to be contextualized against the literature and what you would expect with a small sample." [Tr. Vol. 6, pg 48]. However, it is well-documented in statistical and econometric literature (e.g., "Design and Analysis of Experiments" by A. Den D. Voss, 1999 "Econometric Analysis" Sixth Edition by W.H. Greene, 2008) that a sample of size 244 can be considered to be a large sample.

Hydro One is also concerned with the fairness of AMPCO's proposal. Their "high five" approach amounts to sharing Network costs based on relative contribution to the system peak during heat-waves in summer or cold snaps in winter. During these periods, customers with weather-sensitive load would have a higher share of demand compared to customers with non-weather sensitive load. This is in contrast with the current formulation, in which customer costs depend on their contribution to the 12 monthly peaks, including both weather-sensitive (i.e. summer and winter) and non weather sensitive (i.e. shoulder) months.

Hydro One would like to raise a further concern associated with CME's suggestion that the implementation of the proposal also include a requirement to establish a monitoring and reporting mechanism to demonstrate the extent to which lower electricity prices are being realized as a result of accepting AMPCO's approach. Hydro One is not aware whether there is a method to determine, after the fact, what commodity prices would have been if the Network charge determinants had remained unchanged. The main selling point of AMPCO's proposal is the potential for lower commodity prices that may result from customers shifting load away from the 5 highest peak days. The difficulty is evaluating, in any meaningful way, this assertion.

For the foregoing reasons, Hydro One requests that the Board approve its proposal to maintain the status quo pending further evaluation of AMPCO's proposal if so requested by the Board to permit the Board, stakeholders and Hydro One to evaluate the rate impacts of any change to the Network charge determinants.

All of which is respectfully submitted.

ORIGINAL SIGNED BY D.H. ROGERS

D. H. Rogers

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