

K12.2 1

Ontario Energy Board      Commission de l'énergie  
de l'Ontario



**EB-2009-0096**

**IN THE MATTER OF AN APPLICATION BY  
HYDRO ONE NETWORKS INC.**

**2010 and 2011 DISTRIBUTION RATES**

**DECISION WITH REASONS**

April 9, 2010

Ontario Energy Board	
FILE No.	EB-2010-0008
EXHIBIT No.	K12.2
DATE	October 28, 2010
08/99	

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testing processes. This is a basic tenet of law; in order to succeed an argument must be founded on evidence properly before the decision maker.

The Revised Guideline is clear on its face: parties wishing to challenge the application of the Guideline in whole or in part to any given utility have an obligation to file evidence supporting their point of view. That burden properly rests with the party seeking to displace the operation of the Guideline. Argument, unsupported by evidence, is not the appropriate vehicle for advancing these positions.

In this proceeding the intervenors seeking to challenge the application of the Guideline explicitly chose not to file evidence on these issues. They also did not reference any aspects of the evidence already on the record.

It should also be noted that an attack on the application of the Revised Guideline in the context of a particular rate proceeding, such as this one, does not involve a re-consideration of the Revised Guideline per se. As has been determined in this case in our ruling of December 15, 2009, the Board will not entertain such a re-consideration of the Guideline. What the Board can consider is whether the Guideline or some portion of it ought not to apply to a given utility in the context of a specific cost of service proceeding. In order to succeed, that challenge must be supported by properly introduced evidence. It is for the challenging party to decide what evidence it believes is appropriate to bring, but it may well go beyond a simple assertion respecting transaction costs or the nature of the assets typically funded through the working capital allowance.

For these reasons, the Board finds that the Revised Guideline will be applied to the applicant. This includes implementation of the updated cost of capital parameters, which were issued on February 24, 2010. It also means that the company's cost of long term debt must be updated to reflect the actual debt costs associated with the actual debt instruments used by the company in 2009. In its oral evidence, the company had suggested that such an update would not be undertaken. The Board considers that approach to be inconsistent with the Revised Guideline, which expresses the Board's intention to rely on the actual costs for long term debt, when they are known.

The Cost of Capital parameters will be updated for the purpose of establishing 2011 rates. The Board will rely on September, 2010 data for purposes of deriving the ROE and short-term debt rate. The Board will issue a letter containing the necessary values to allow Hydro One to develop a Draft Rate Order, to be effective January 1, 2011.

Hydro One will be required to provide an updated cost of long-term debt, based on actual debt issued. The Board expects this process to be mechanistic in nature; no further evidence will be heard at that point.

Ontario Energy  
Board

Commission de l'énergie  
de l'Ontario



EB-2007-0680

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

**AND IN THE MATTER OF** an application by Toronto  
Hydro-Electric System Limited for an order approving or  
fixing just and reasonable rates and other charges for the  
distribution of electricity to be effective May 1, 2008, May  
1, 2009, and May 1, 2010.

**BEFORE:** Paul Sommerville  
Presiding Member

Paul Vlahos  
Member

David Balsillie  
Member

**DECISION**

**May 15, 2008**

## 8. Implementation

### 8.1 Cost of Capital Update

In mid-2006, the Board initiated a consultative process to examine the cost of capital applicable to the Ontario electricity distribution sector. This process was conducted in conjunction with the development of the 2nd Generation Incentive Regulation plan. The product of these consultations was the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors* (the "Board Report"), issued December 20, 2006. The Board Report considered the extensive consultation record and established, in part, guidelines for setting and updating the cost of capital parameters for distribution rate-setting from 2007 onwards, including the return on common equity ("ROE"), the deemed short-term debt rate, and, as appropriate, the deemed long-term debt rate.

The Board Report established that the approved ROE to be used for rate-setting purposes should be calculated by application of the formula in Appendix B of the Board Report. In setting the ROE for the establishment of 2008 rates, the Board has used the Consensus Forecasts and published Bank of Canada data for January 2008, in accordance with the Board's guidelines. In fixing new rates and charges for Hydro 2000 the Board has applied the policies described in the Board Report. Based on the final 2007 data published by Consensus Forecasts and the Bank of Canada, the Board has established the ROE for 2008 to be 8.57%.

The Board Report also established that the short-term debt rate should be updated using the methodology in section 2.2.2 of the Board Report. The Board has set the short-term debt rate at 4.47% using data from Consensus Forecasts and the Bank of Canada for January 2008.

Based on the above updates and in accordance with the settlement agreement, for purposes of setting 2008 rates, the Board-approved capitalization and cost of capital for the Applicant is as follows:

**Table 15**  
**Board-approved 2008 Capitalization and Cost of Capital**

Capital Component	% of Total Capital	Cost (%)
Short-Term Debt	4.0	4.47%
Long-Term Debt	58.5	5.48%
Common Equity	37.5	8.57%

## 8.2 Draft Rate Order

This Decision will result in the approval of rates for test years 2008 and 2009. The Board has made numerous findings throughout this Decision which would change the revenue requirements and deficiency claimed by Toronto Hydro for 2008 and 2009. The Board has also made certain findings regarding the disposition of balances in deferral and variance accounts. Further, the Board has made findings on cost allocation and rate design matters that would further affect the rates for certain rate classes. These are to be properly reflected in a Draft Rate Order incorporating an effective date of May 1, 2008 for the new rates.

As the Applicant's current rates were declared interim as of May 1, 2008, given the date of this Decision there will be a difference between the revenue collected under the existing rates and the revenue that would have been collected if the new rates were implemented May 1, 2008. Depending on the date of implementation of the new rates, the new rates shall be set so as to recover the annualized revenue requirement over the remaining period of the 2008 rate year. For example, if the Applicant will be able to implement the new rates on June 1, 2008, the new rates shall reflect the fact that there will be only 11 months to April 30, 2009.

As for 2009 rates, this Decision will govern the establishment of those rates subject to the cost of capital parameter updates and possibly other Board decisions that might apply. The Applicant shall apply in a timely fashion to receive approval for the 2009 rates to be effective May 1, 2009.

In filing its Draft Rate Order for 2008 rates, the Company should attach appropriate documentation in support of its rates, disposition of deferral/variance accounts, disposition of other amounts, and the allocation of the approved revenue requirement to the rate classes.



# ONTARIO ENERGY BOARD

FILE NO.: EB-2009-0069

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VOLUME: 1

DATE: April 3, 2009

Paul Vlahos

Presiding Member

1 MR. VLAHOS: Thank you, Mr. Millar. Anyone else?

2 There being no response, Mr. Roger, I guess I will  
3 turn over to you. Do you have any preliminary matters, Mr.  
4 Millar, before I turn I told over to --

5 MR. MILLAR: I don't believe so.

6 MR. VLAHOS: Mr. Roger.

7 **OPENING STATEMENT BY MR. RODGER:**

8 MR. RODGER: Thank you, Mr. Chairman. By way of  
9 introduction and pursuant to Procedural Order No. 1, issued  
10 by the Board on March 18th, 2009, the matters before the  
11 Board today combine three separate applications made by  
12 Toronto Hydro-Electric System that the Board has determined  
13 will consider at one hearing today. The three applications  
14 are as follows. First on December 15th, 2008, Toronto  
15 Hydro-Electric System made an application seeking approval  
16 to refund revenues derived from the extension of various  
17 rate riders beyond their original expiry and to the first  
18 three months of the 2009 rate year. Toronto Hydro  
19 requested that the refunds be effected to rate riders  
20 commencing May 1st, 2009. These amounts are termed  
21 "expired rate rider excess revenues" and this application  
22 was assigned docket number EB-2008-0402.

23 Secondly, Toronto Hydro-Electric System made a further  
24 answer on March 2<sup>nd</sup>, 2009 for disposition of the 2006 and  
25 2007 amounts in the smart meter deferral account. This  
26 application was directed by the board in its EB-2008-0138  
27 decision on motion and involves disposition of amounts  
28 related to 2006 costs carried over for later recovery, and



1 amounts related to 2007 smart meter activities. The smart  
2 meter deferral account application has docket number EB-  
3 2009-0069.

4 Finally, Toronto Hydro-Electric System filed an  
5 application March 16th, 2009, pursuant to the Board's EB-  
6 2007-0680 decision which approved Toronto Hydro rates for  
7 2008 and 2009.

8 This hearing today concerns the 2009 rate update  
9 application which, among other things, involves the  
10 mechanistic update of Toronto Hydro's cost of capital.  
11 Collectively, the applications request both rate increases  
12 and rate decreases.

13 The combined impact of the updated base distribution  
14 rates and the customer credits arising from these three  
15 applications is that a typical residential customer  
16 consuming a thousand kilowatt hours per month will have a  
17 bill increase of approximately \$1.11, or about 1 percent on  
18 the customer's total bill.

19 For your ease of reference, Mr. Chair, we produced a  
20 binder that is a compendium of all three applications and I  
21 wonder if we could have this marked as an exhibit, sir?

22 MR. MILLAR: As Exhibit K1.1, and I'll bring up a copy  
23 forward.

24 EXHIBIT K1.1: COMPENDIUM OF TORONTO HYDRO'S THREE  
25 APPLICATIONS

26 MR. RODGER: Thank you, Mr. Millar. Also, Mr.  
27 Chairman, in Procedural Order 1, it provided for  
28 interrogatories to be submitted to Toronto Hydro and we

1 was not accepted. I think the issue Mr. Warren was raising  
2 was where did this come from. Was the utility putting  
3 forward this for the first time now, and our point is, no,  
4 this was part of our last re-basing application.

5 MR. VLAHOS: Mr. Rodger, I'm just a little concerned  
6 about the assumption that you are working with. The  
7 company files 10,000 pages. Just because the Board, or  
8 intervenors at the Board does not addressing every word of  
9 it, means that -- it was pre-filed therefore -- the Board  
10 didn't say anything, and therefore it is approved. I'm a  
11 little concerned about that line of it.

12 MR. RODGER: Fair enough.

13 MR. VLAHOS: Mr. Buonaguro? Don't re-argue this.

14 MR. BUONAGURO: I was just looking, he mentioned the  
15 evidence reference I was looking through the reference to  
16 30 years. I just noted that the second city note repayment  
17 in the evidence was for 10 years. It was suggested they  
18 might be doing it for 10 years, not 30 years.

19 It also says the first note was for 30 years and I  
20 think they ended up doing 10 years, so it's not as clear-  
21 cut as it might seem.

22 MR. VLAHOS: Okay. The panel is excused. Many  
23 thanks. Can we take 10 minutes, please.

24 --- Recess taken at 2:55 p.m.

25 --- On resuming at 3:10 p.m.

26 MR. VLAHOS: The good news is that there is no  
27 dissenting in this opinion.

28 DECISION:

1 MR. VLAHOS: On December 2nd, 2008, Toronto Hydro  
2 filed an application for authorization for two things:  
3 first, to dispose of amounts, both positive and negative,  
4 derived from the continued existence of rate ride that were  
5 to have expired on April 30th, 2008, but which were  
6 continued until July 31st, 2008; and two, to implement the  
7 resulting adjustments by way of rate riders effective for  
8 the 2009 rate year over a 12-month period commencing May  
9 1st, 2009.

10 The following rate riders were to have expired on  
11 April 30th, 2008, but which were continued until July 31<sup>st</sup>,  
12 as I mentioned, and this was done by Board authorization:

13 A, 2006 lost revenue adjustment mechanism, six-month  
14 rate rider; B, 2006 shared services mechanism, six-month  
15 rate rider; C, 2006 smart meter six-month rate rider; and  
16 D, regulatory assets recovery account rate rider.

17 That is the first application that the Board dealt  
18 with today.

19 The second application relates to the filing by  
20 Toronto Hydro on March 2nd, 2009. It was an application  
21 for disposition for two things. First: disposition of the  
22 2007 year-end balances or balance in this smart meter  
23 deferral account together with a residential balance in the  
24 2006 smart meter deferral account, totalling a net credit  
25 to customers of \$743,500; and second, approval of smart  
26 meter rate rider values for 2009 to take effect May 1st,  
27 2009.

1           The third application that was heard today relates to  
2 a request filed on March 16th, 2009, where Toronto Hydro  
3 filed an application to reflect in rates effective, again,  
4 May 1st, 2009, updated cost of capital values as it was  
5 required to do pursuant to the Board's May 15th, 2008,  
6 decision, which decision dealt with two test years, 2008  
7 and 2009.

8           The draft rate order that was filed by Toronto Hydro  
9 as part of its pre-filed evidence also included the  
10 additional tariff sheets that relate to the first two  
11 applications that I noted earlier.

12           The Board had determined that it will combine those  
13 three applications to one, which was pursuant to subsection  
14 21(5) of the Ontario Energy Board Act.

15           For purpose of this proceeding, the Board also adopted  
16 the list of intervenors that were approved in the most  
17 recent Toronto Hydro main rates proceeding noted earlier,  
18 which was for rates for 2008 and 2009. The file number on  
19 that was EB-2007-0680.

20           The Board proceeded by way of an oral hearing which  
21 was the purpose of today and allowed a process for  
22 interrogatories; which Board Staff, I believe, were the  
23 only party that did ask IRs which were responded by the  
24 applicant.

25           Having heard the evidence and the arguments by  
26 parties, there are two things here that I need to pronounce  
27 on. One is the cost rate itself of the debt instrument,  
28 and secondly, the timing of that debt instrument. So I

1 will do so, and I may also comment along the way on some of  
2 the things that have come up, if not as findings, but at  
3 least as commentary that may be of assistance to the  
4 parties going forward.

5 The starting with the cost rate itself, the proposed  
6 rate is 7.25 percent and it is based on a 30-year term. We  
7 heard -- the Board heard argument today about the  
8 reasonableness of that cost rate. There was some  
9 discussion whether the 10-year term would have produced a  
10 lower rate or not, but this item was not pursued by  
11 intervenors in their arguments.

12 It also assisted the Board with the witnesses  
13 clarifying their position, which is now acceptance of the  
14 notion, or the principle, that whatever the Board may  
15 approve by way of forecast cost of debt, there will be an  
16 opportunity in the next cost-of-service review when the  
17 actual rate itself is brought forward, the contracted rate,  
18 for the parties to consider that rate, the reason for that  
19 rate and it would be open to the intervenors to argue  
20 accordingly.

21 So with that understanding, that there will be an  
22 opportunity, and that opportunity was agreed to by all,  
23 that it will be the 2011 cost-of-service review proceeding,  
24 the Board will accept the 7.25 percent proposed forecast  
25 rate on two grounds: one, that it is not inconsistent with  
26 the settlement proposal reached by the parties that the  
27 company shall present a forecast rate; and two, the rate

14

1 itself, the level of the rate is below the Board's own  
2 values that have been announced.

3 I turn to one argument, by CCC specifically. It is my  
4 conclusion that what the company proposes is not  
5 inconsistent with the settlement proposal.

6 It is also my view that the IRM process, if that's was  
7 being contemplated as being the home for this review, this  
8 prudence review of the debt rate, the IRM process was not  
9 intended for that purpose. That's not to say that someone  
10 cannot argue differently before another panel when that  
11 time arrives, and this is just by way of commentary.

12 Now, we've come to the second issue, and that is the  
13 timing of the debt instrument. The utility's proposal or  
14 its draft rate order reflects a revenue requirement which  
15 reflects an October 1st proposed date. However, the money  
16 to be paid to its parent it's not due until December 31st,  
17 2009.

18 Therefore, there is a time where the -- based on the  
19 company's proposal, where there will be monies raised with  
20 those monies not finding a home for three months. The  
21 result of that is there is some impact on the revenue  
22 requirement that is effected in the submitted draft rate  
23 order. The issue is what to do -- what should the Board do  
24 with that difference in the revenue requirements.

25 There were various suggestions from decreasing the  
26 revenue requirement, that is directing the company to  
27 prepare another rate order to reflect a decrease up to a  
28 million dollars or the company simply to make its case the

1 next time and be prepared to refund some of those monies,  
2 up to a million dollars, to its customers and then counsel  
3 to Board Staff noted you can't do that unless you have a  
4 deferral account, a variance account; a fair point.

5 My conclusion is that it would be a lot cleaner and  
6 more principled, if the draft rate order were to be revised  
7 to reflect a reduction in the revenue requirement for the  
8 2009 year, because of the time consideration between  
9 October 1st and December 31st.

10 The issue, is to what would be a reasonable number of  
11 days prior to December 31st, and I heard the witnesses  
12 today, when asked about mid-December, whether that is  
13 reasonable, and the answer was it's doable.

14 I wasn't sure whether we have the precise amount, that  
15 I can say: The revenue requirement shall be reduced by X  
16 amount or by an amount that would correspond from October  
17 1st to December 15th. I don't want to complicate the  
18 world. It's a bit of a half-decision, because I may want  
19 to just canvass this a bit more, Mr. Rodger.

20 Do we have an amount on record, Mr. Millar, for  
21 December 15th?

22 MR. MILLAR: We don't for December 15th. We have  
23 December 1st and December 31st. I'm not sure if it's as  
24 simple as splitting the difference, but maybe Mr. Sardana  
25 can comment.

26 MR. SARDANA: Well, if it assists, we can certainly  
27 provide that number. Obviously, you know, I'd need a few  
28 minutes to go back to my spreadsheet, and Mr. Seal and I

»Accounting  
»Part V – Pre-changeover accounting standards  
»Accounting Standards  
»Specific items [Sections 3000 — 3870]  
»3110 - Asset Retirement Obligations

## **SPECIFIC ITEMS**

### **SECTION 3110**

#### **asset retirement obligations**

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**Additional  
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**Background  
Information and  
Basis for Conclusions**

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#### **PURPOSE AND SCOPE**

- .01 This Section establishes standards for the recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated asset retirement costs.



- .02 This Section applies to legal obligations associated with the retirement of a tangible long-lived asset that result from its acquisition, construction, development or normal operation. This Section covers the obligations of both lessors and lessees in connection with leased assets, whether imposed by a lease agreement or by a party other than the lessor, except for those obligations of a lessee that meet the definition of either minimum lease payments or contingent rentals in LEASES, Section 3065, and are accounted for in accordance with that Section. This Section also covers obligations arising in connection with leasing and other agreements concerning the rights to explore for or exploit natural resources, to which LEASES, Section 3065, does not apply. This Section does not apply to:
- (a) obligations that arise solely from a plan to sell or otherwise dispose of a long-lived asset subject to DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475; and
  - (b) obligations that result from the improper operation of an asset.

#### DEFINITIONS

- .03 The following terms are used in this Section with the meanings specified:
- (a) An **asset retirement obligation** is a legal obligation associated with the retirement of a tangible long-lived asset that an entity is required to settle as a result of an existing or enacted law, statute, ordinance or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel.
  - (b) **Retirement** of a long-lived asset is its other-than-temporary removal from service, including its sale, abandonment, recycling or disposal in some other manner, but not its temporary idling.
  - (c) **Fair value** is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.
  - (d) An **asset retirement cost** is the amount that is capitalized and increases the carrying amount of a long-lived asset when a liability for an asset retirement obligation is recognized.
  - (e) A **credit-adjusted risk-free rate** is the rate of interest on monetary assets that are essentially free of default risk, adjusted for the effect of an entity's credit standing.
  - (f) **Accretion expense** is the increase in the carrying amount of an asset retirement obligation due to the passage of time.
- .04 Promissory estoppel is the legal principle that a promise or assurance made without consideration may nonetheless be enforced to prevent injustice when:
- (a) the promise or assurance was intended to affect a contract or other legal relationship between the promisor and the promisee, and to be acted on; and
  - (b) the promisee acted on the promise or assurance, or in some way changed its position.

#### INITIAL RECOGNITION AND MEASUREMENT

- .05 ♦ *An entity should recognize the fair value of a liability for an asset retirement obligation in the period in which it is incurred when a reasonable estimate of fair value can be made. If a reasonable estimate of fair value cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when a reasonable estimate of fair value can be made. [JAN. 2004]*