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April 13, 2012

BY EMAIL & COURIER

Ms. Kirsten Walli  
Board Secretary  
Ontario Energy Board  
2300 Yonge St, Suite 2701  
Toronto ON M4P 1E4

Dear Ms. Walli:

**Board File No. EB-2011-0271**  
**Halton Hills Hydro Inc. – 2012 Cost of Service Application**  
**Energy Probe – Argument**

Pursuant to Procedural Order No. 5, issued by the Board on March 26, 2012, attached please find the Final Argument of Energy Probe Research Foundation (Energy Probe) in the EB-2011-0271 proceeding for consideration by the Board.

Should you require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh  
Case Manager

cc: Arthur Skidmore, Halton Hills Hydro (By email)  
David Smelsky, Halton Hills Hydro (By email)  
Richard King, Norton Rose LLP (By email)  
Randy Aiken, Aiken & Associates (By email)  
Intervenors of Record (By email)

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**Ontario Energy Board**

**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 Halton Hills  
Hydro Inc. for an Order or Orders approving of fixing just and  
reasonable rates and other charges for the distribution of  
electricity as of May 1, 2012.

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**ENERGY PROBE RESEARCH FOUNDATION  
("ENERGY PROBE")**

**ARGUMENT**

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**April 13, 2012**

**HALTON HILLS HYDRO INC.  
2012 RATES**

**EB-2011-00271**

**ARGUMENT OF ENERGY PROBE RESEARCH FOUNDATION**

**A - INTRODUCTION**

This is the Argument of the Energy Probe Research Foundation ("Energy Probe") related to the setting of 2012 rates for Halton Hills Hydro Inc. ("HHH") effective May 1, 2012.

HHH filed a Partial Settlement Agreement with the Board on February 28, 2012. This Partial Settlement Agreement was accepted by the Board at the commencement of the oral hearing on March 22, 2012.

The list of unsettled issues in this proceeding is as follows:

- \* Green Energy Initiative - the inclusion of one capital project in capital expenditures in the test year (including the resulting impacts on depreciation, PILS, cost of capital, loss factor, etc.);
- \* PP&E Deferral Account - the appropriate amount included in the account and the amortization period;
- \* Deferral and Variance Account Clearance;
- \* Long-Term Debt Rate; and
- \* OM&A costs.

Energy Probe makes submissions on each of these issues in the sections that follow.

Energy Probe notes that in their Argument-In-Chief, HHH states that the context for the disposition of the unresolved issues is a bottom line request by HHH for "*a very modest - almost negligible - increase in rates*" (Argument-in-Chief dated March 30, 2012, paragraphs 3-8). As part of their submission, HHH appears to believe that the reduction in the return on equity and the deemed long-term debt rate, which are the result of the Board's March 2, 2012 update, should be taken into account when the Board determines the unresolved issues.

Apparently, in the view of HHH, the reduction in the deficiency from about \$209,000 to \$79,000 as a result of the changes in the cost of capital parameters should somehow influence the Board on the level of OM&A, the calculation of the appropriate long-term debt rate, the amortization of the PP&E deferral account and the inclusion of the Green Energy Initiative project in rate base. Energy Probe respectfully disagrees. The remaining unresolved issues should be determined based on the evidence for each of the issues.

HHH further appears to be under the impression that a cost of service application should result in an increase in rates. Energy Probe notes that while this is often the case, there are situations in which rates decrease as the result of a cost of service rebasing application. This can be driven, as in the case of HHH, by strong customer growth, significant reductions in the cost of long and short-term debt and effective cost control on OM&A expenses.

Energy Probe does not believe, for example, that approved OM&A expenses can be allowed to increase simply because the long-term debt rate has fallen resulting in a lower cost of debt component in the revenue requirement. HHH would likely agree that if the long-term debt rate increases in the future, increasing the cost of debt in the revenue requirement, that should not be used as a reason for a decrease in OM&A expenses.

## **B - GREEN ENERGY INITIATIVE**

### **i) HHH Proposal**

HHH's Green Energy Initiative ("GEI") capital project has been described in Exhibit 2, Tab 3, Schedule 7 and will not be repeated here. In their Argument-in-Chief (paragraph 11) HHH indicates that the revenue requirement associated with the GEI is \$91,467, as noted in the response to Energy Probe Interrogatory #19. Energy Probe disagrees. The calculation of the revenue requirement that arises from the GEI underwent a number of revisions and corrections throughout this proceeding. The response to Energy Probe Interrogatory #55 provided a detailed breakdown of the costs that were stated in the response to Energy Probe Interrogatory and resulted in a small increase in the revenue requirement to \$92,359. The response to Energy Probe Technical Conference Question #2 provided a correction to the PILS calculation and resulted in a revenue requirement of \$82,111. However, as discussed at the oral hearing (Tr. Vol. 1, pp. 53-54) this figure did not include any OM&A costs and did not reflect the updated cost of capital that resulted from the Board's March 2, 2012 letter.

Energy Probe notes that HHH has filed a response to Undertaking J1.4 that reflects the addition of the OM&A costs and the updated cost of capital parameters. However that response also includes the increase in the Capital Cost Allowance ("CCA") from that proposed by HHH of \$56,000 (Table EP TC-1 in Energy Probe Technical Conference Question #2) to \$350,000 as requested in the undertaking.

To complete the record, Energy Probe has provided the calculation of the impact on the revenue requirement that reflects the response to Undertaking J1.4, but with a CCA of \$56,000 as proposed by HHH. This table has been attached to this submission as Appendix A and reflects a revenue requirement of \$89,911 for the test year.

HHH's evidence and Argument-in-Chief lists a number of benefits of the GEI to ratepayers including reduced non-commodity charges (transmission, global adjustment), and power purchases. HHH quantified these savings in Table EP 2-5 in the response to Energy Probe Interrogatory #55. Energy Probe accepts these estimated savings of \$35,495 as being reasonable. The net impact, therefore, is an increase in costs to ratepayers of \$54,415.

HHH notes that there are other benefits to ratepayers that would result from the GEI. Unfortunately many of these benefits are simply stated in the Argument-in-Chief and are not contained in the evidence. HHH was asked to provide the cost benefit analysis of the GEI project and the cost savings noted above of \$35,495 were provided. There was no mention of any other benefits that would accrue to ratepayers. In fact, the deferral account being requested by HHH into which the benefits to ratepayers would accrue provides no mention of these other benefits which have not been quantified.

Mr. Skidmore did identify one other benefit to ratepayers that had not been quantified (Tr. Vol. 1, page 53). That was the benefit of peak demand savings. However, as shown in the response to part (a) of Energy Probe Interrogatory #55, these peak savings would be less than 400 kW, a de minimis amount, similar to the reduction in the loss factor associated from the GEI project from 6.02% to 6.01% as calculated in the response to part (g) of Energy Probe Interrogatory #19.

Energy Probe notes that the response to Undertaking J1.3 does not include a study that evaluates actual results in any form of a cost benefit analysis. In the response provided in addition to the study, HHH indicates that the decision to proceed with the GEI was made based on their pilot project experience as well as discussions with individuals at other utilities. HHH has not made any of that information available to parties in this proceeding and apparently they have not been able to quantify any benefits other than those shown in Table EP 2-5 in Energy Probe Interrogatory #55.

The GEI project as proposed results in a net cost to ratepayers in the 2012 test year of \$54,415. Over a four year cycle of rebasing and IRM, this results in ratepayers paying nearly \$360,000 (4 x \$89,911) to receive less than \$142,000 (4 x \$35,495) in cost savings. It is submitted that this is a bad deal for ratepayers. At the same time, Energy Probe notes that based on the response to Undertaking J1.4-Revised, HHH's shareholder will receive a return on equity of \$25,000 each year for these four years for a total after tax return of \$100,000.

The impacts on ratepayers are even more severe after the first four years. Energy Probe has provided a version of the response to Undertaking J1.5 - Revised at Appendix B to this submission that reflects a small change in the deemed interest expense and the deemed return on equity so that the figures match those in Undertaking J1.4 - Revised. The major change between Appendix B and the table in Undertaking J1.5 - Revised is the CCA. Energy Probe has used the 8% proposed by HHH in place of the 50% requested by Energy Probe for the undertaking.

Appendix B shows that the impact on ratepayers is an increase in the revenue requirement after taking into account the savings to ratepayers from \$54,415 in the first four years to \$119,306 in years 5 through 8, \$101,822 in years 9 through 12, \$82,831 in years 13 through 16, and \$62,657 in years 17 through 20. The net present value of this additional cost is more than \$390,000.

Based on the above analysis of the impact on the ratepayers, Energy Probe submits that the Board should not approve the GEI project as proposed by HHH. The project does not pass a cost benefit analysis for ratepayers and HHH has not provided any evidence to suggest that the benefits that have not been quantified would be greater than the current shortfall in the analysis.

#### **ii) CCA Adjustment to HHH Proposal**

Energy Probe submits that if the Board were to approve the inclusion of the GEI in the 2012 revenue requirement, the Board should consider how HHH should deal with the CCA calculation for PILs purposes. The HHH proposal uses a CCA rate of 8% that is based on classifying the solar assets as distribution assets in Class 49 (Energy Probe Technical Conference Question #2b). When asked why HHH had not used Class 43.2 with a 50% CCA rate, Mr. Skidmore stated that "*the fast write-off of 43.2 is more from an experimental nature, and in our opinion this isn't experimental*" (Technical Conference Tr. Vol. 1, page 6).

Mr. Skidmore explained that he was aware that CCA Class 43.2 with a rate of 50% was designed to provide enhanced tax deductions for various renewable asset properties (Tr. Vol. 1, page 55). However he believed it was more appropriate to treat these assets as distribution assets.

Energy Probe notes that the Board has a long history of regulating utilities in Ontario and has been consistent in requiring those utilities to maximize their deductions, including CCA, for tax purposes in order to both minimize the revenue requirement and to minimize the intergenerational inequity of delaying tax deductions to future rates. The Board has required utilities to use the maximum CCA deduction for assets that have accelerated write-off for tax purposes such as computers, software and vehicles even though these assets usually have useful lives in excess of the period when the costs are written off for tax purposes.

Energy Probe notes that in the response to Undertaking J1.5 - Revised, the resulting revenue requirement in years 1 through 4 of using the maximum allowed CCA deduction for PILs purposes reduces the net cost to ratepayers to \$8,810 per year from the \$54,415 increase based on the HHH proposal. While this is better for customers in the immediate term, the net present value of using the accelerated CCA increases the net present value of the additional costs to more than \$500,000 from the \$390,000 shown in Appendix B.

This differential will vary depending on the discount rate used and the cost of capital assumptions used every time HHH rebases and on the continuation of the four year rebasing cycle shown, but directionally it will remain unchanged. In short, the CCA deduction can provide a reduced impact on customers now if the maximum CCA is used but this results in a greater NPV impact on customers over 20 years than if the lower CCA proposed by HHH is used.

Energy Probe submits, therefore, that if the Board allows inclusion of the GEI in rate base, it should deviate from its standard practice of requiring the maximum CCA deduction to be taken for PILs purposes. If the utility did take the maximum deduction it was entitled to in the first four years, most of this benefit would flow to the shareholder through significantly lower taxes in years 2 through 4 than were built into the test year rates. Similarly the 8% CCA rate proposed by HHH is not appropriate as it results in a significant unused CCA deduction of more than \$230,000 (\$1,400,000 less accumulated CCA of \$1,146,396 shown in Appendix B) in year 21, which is the end of life for these assets.

Energy Probe notes that a CCA rate of 29% (midpoint of 8% and 50%) would result in an increase in the costs to ratepayers in years 1 through 4 of about \$31,500 per year, while increasing the net present value of the 20 year costs to ratepayers to about \$463,000. The Board may wish to consider this or some other alternative to balance the short and long term cost consequences to ratepayers of the GEI project.

Regardless, Energy Probe submits that if the Board allows the inclusion in rate base of the GEI project, it should direct HHH to use a specific CCA rate for tax purposes not only for the test year but also for the following IRM years. HHH is free to use the 50% accelerated rate for PILs purposes but if it were to do so in any of those years, the shareholder would benefit through higher after tax retained earnings, while upon rebasing, the tax deduction would be significantly used up, resulting in higher PILs to be included in the revenue requirement and being paid for by ratepayers. Member Spoel hinted at potential concerns related to the CCA rate to be used (Tr. Vol. 1, pp. 57-59). On behalf of ratepayers, Energy Probe echoes those concerns.

### **iii) Alternatives to Consider**

As noted above, Energy Probe submits that the Board should not approve the addition of \$1.4 million to rate base and the resulting impacts on depreciation expense, PILs, cost of capital, loss factors, etc., in the test year revenue requirement because HHH has not proven its case that there is a benefit to ratepayers.

However, Energy Probe believes there are a number of alternatives that the Board may wish to consider other than simply yes or no to the GEI if the Board believes that there may be benefits to ratepayers. Energy Probe provides a number of possible alternatives for the Board to consider, along with a brief description of them.

\* Scaled Down Pilot Project - HHH has not provided any quantifiable benefits to ratepayers associated with the benefits noted paragraph 12 of their Argument-in-Chief. Energy Probe submits that 100 installed panels, at a cost of approximately \$100,000 should be large enough for HHH to collect data and information over a number of years and provide the results to the Board and interested parties as part of its next rebasing application. All parties would then be in a better position to evaluate the savings potential of this project.



\* Time Horizon Option - Rather than installing 1,400 panels in 2012 with another potential 1,400 panels at some future time (Tr. Vol. 1, page 47) creating a lumpy investment cycle over the 20 year life of these assets, the Board may wish to consider the approval to include 140 installations in the test year (2,800 total divided by 20 year life). This option has a significantly lower rate impact on ratepayers that would be phased in over 20 years and eliminates the potential lumpy capital expenditures 20 years from now in the replacement of 1,400 installations made this year under the HHH proposal.

\* Allow the installation of all 1,400 panels in the test year, but deem the deferral account that is to record the cost savings to ratepayers to be equal to the increase in the revenue requirement each year over the 20 year life of the installations. The Board would essentially be approving non-quantified benefits identified by HHH that would equal to the quantified shortfall. The benefit of this approach is that there is no impact on ratepayers in either the short or long-term. HHH gets to earn a return on the assets and the actual and deemed savings offset the associated costs of the assets (return on equity, cost of debt, depreciation, PILs, OM&A, losses, etc.). If HHH believes that the project is in the best interest of ratepayers, then this alternative should be acceptable to them as it leaves ratepayers indifferent as far as their rates go in both the short and long-term.

## **C - PP&E DEFERRAL ACCOUNT**

### **i) Quantum**

HHH updated the amount in the PP&E deferral account prior to the oral proceeding reducing the amount to be refunded to ratepayers from \$1,462,823 to \$836,717. HHH did not, however, provide a complete evidentiary record of the changes in the calculation of rate base for 2011 under CGAAP and MIFRS. HHH only indicated that it had corrected an error in the calculation of the depreciation expense under CGAAP (Tr. Vol. 1, page 11). In response to Undertaking J1.1 HHH has provided a continuity statement for 2011 under CGAAP that shows the depreciation expense. Based on this response, Energy Probe has assembled the following data from that undertaking response and from Tables 2-7 through 2-9 in Exhibit 2, Tab 2, Schedule 1. These tables are the continuity schedules for 2008 through 2010 in CGAAP.

<b><u>CGAAP Depreciation</u></b>			
	Gross Assets	Depreciation	As % of
<u>Year</u>	<u>Closing Balance</u>	<u>Expense</u>	<u>Closing Balance</u>
2008	44,489,081	2,156,324	4.85%
2009	44,433,150	2,244,642	5.05%
2010	46,293,583	2,379,251	5.14%
2011	49,126,366	2,115,000	4.31%

As shown in the above table, there has been a sudden and abrupt change in the depreciation calculated under CGAAP in 2011 as compared to the previous years. In 2008 through 2010 the depreciation expense as a percentage of the closing balance of gross assets rose from 4.85% to 5.14%. In 2011 it suddenly drops to 4.31%, a level not seen in the previous three years. On a dollar basis, the depreciation expense increased by more than \$220,000 between 2008 and 2010 reflecting the increase in gross assets that took place over the same period. In 2011, however, the depreciation expense falls by more than \$260,000, or 11.1%, from that recorded in 2010, despite an increase \$2.8 million, or 6.1% in the value of gross assets.

While circumstances may exist where the depreciation amount and the percentage of total gross assets may decrease even when gross assets are increasing (such as short lived assets such as computers, software etc. being fully depreciated), HHH has not provided any evidence that this is the case.

As a result, Energy Probe is not able to accept that the depreciation expense calculation for 2011 under CGAAP is correct, as the above table shows a discontinuity in the CGAAP based figures between 2008 and the revised and untested 2011 figures.

Energy Probe invites HHH to respond to this apparent discontinuity in Reply Argument. Energy Probe would first ask HHH to confirm that the depreciation rates used in calculating the 2011 depreciation expense under CGAAP are unchanged from those used in 2008 through 2010.

Second, Energy Probe notes that the reduction in the 2011 CGAAP depreciation expense noted in the March 21, 2012 letter is approximately \$625,000. Energy Probe notes that the changes appear to be spread over most, if not all of the line items in the 2011 continuity schedule. However, as shown in the following table, two line items stand out when compared to the depreciation expense booked in 2008 through 2010 and account for more than the total change noted in the March 21, 2012 update. The data for 2008 through 2010 have been taken from Tables 4-19 through 4-21 in Exhibit 4, Tab 2,

Schedule 7. The 2011 data is taken from the CGAAP continuity schedule provided in the response to Undertaking J1.1.

<b><u>CGAAP Depreciation</u></b>		
	Account 1830	Account 1995
	<u>Poles, Towers</u>	<u>Contributions</u>
<u>Year</u>	<u>&amp; Fixtures</u>	<u>&amp; Grants</u>
2008	1,298,707	-172,718
2009	1,310,741	-180,402
2010	1,354,025	-166,484
2011	<u>749,437</u>	<u>-236,516</u>
2011 vs 2010	-604,588	-70,032

Energy Probe invites HHH to explain the significant reduction in the depreciation expense shown in 2011 for account 1830 and the significant increase in the offset to the depreciation expense shown in 2011 for account 1995.

Finally, Energy Probe invites HHH to explain any other significant differences in depreciation expenses that it has calculated for 2011 under CGAAP relative to the 2010.

## **ii) Amortization Period**

HHH is proposing to amortize the PP&E deferral account over 20 years as noted in the Match 21, 2012 update letter. As the Board is aware, other distributors have amortized the PP&E deferral account over a period of four years, a significantly shorter time horizon than that proposed by HHH. This four year period also aligns with the length of the IRM term of a year for rebasing followed by 3 years of IRM.

In the EB-2008-0408 Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment dated June 13, 2011 the Board stated, at page 32, that:

*"The Board will determine the period of time for amortization on a case-by-case basis and will be guided primarily by such considerations as the impact on rates, implications of any other IFRS transition matters and any requirements for rate mitigation."*

In their Argument-in-Chief HHH indicates that amortizing the account over 20 years would have an effective reduction in rates of 0.4%, whereas amortizing the account over four years would effectively reduce rates by 2% per year. HHH also argues that there is no need for rate mitigation in the context of this rate application because only a modest rate increase is being sought.

In its evidence (March 21, 2012 letter), HHH provided three reasons for its proposal: minimizing intergenerational inequity, minimizing rate volatility and significant cash flow impacts to HHH.

Energy Probe submits that none of the reasons provided by HHH support their request for a 20 year amortization period. Energy Probe submits that the Board should set the amortization period to four years so that when HHH comes back in for its next rebasing application, this deferral account will be fully amortized.

On the first issue of minimizing intergenerational inequity, Energy Probe disagrees with the submissions of HHH, with the exception that as a rate making principle, intergenerational inequity means that one generation of customers should not be forced to cover the costs of another generation of customers. A 20 year amortization period can cover several generations of customers. Many customers today will not be customers in 20 years and there will be many customers in the future that are not customers today. While this is true for residential customers, it is even more relevant for commercial and industrial customers. Most of the commercial and industrial customers of HHH today did not even exist 20 years ago in 1992. Similarly, HHH has many residential customers today that were not customers in 1992. Customers cannot and should not be considered to be homogenous over a 20 year period.

The updated evidence of March 21, 2012 provides a net present value calculation of the HHH proposal (Option 1) compared to the four year amortization (Option 3). This clearly demonstrates that the net present value of the HHH proposal is inferior to the four year amortization approach. Energy Probe notes that HHH has used a discount rate of 6.2%, equal to their overall after-tax cost of capital. If this discount rate was increased to reflect a social discount rate or a before-tax cost of capital (since residential customers do not get to subtract the cost of the utilities when they pay income tax), the differential would be even greater than that shown.

Energy Probe submits that the HHH proposal increases intergenerational inequity. Customers are being told to pay more now under the HHH proposal because of the change from CGAAP to MIFRS so that future customers can pay a little less.

HHH claims that a 20 year amortization aligns with the useful lives of the distribution assets. Energy Probe notes that the smart meter rate disposition rider will collect approximately \$1.3 million over four years, and not over the remaining useful lives of the smart meters. The only difference is that HHH wants to collect this money from ratepayers over a four year period for smart meters and refund money to the same ratepayers over a 20 year period to enhance their cash flow. If intergenerational equity was a true concern of HHH it should not be limited to those instances where it benefits the utility to the detriment of ratepayers.

With regard to the second reason for the proposal of minimizing rate volatility, Energy Probe once again disagrees with HHH and submits that the HHH proposal actually increases rate volatility. The following table shows the amounts to be collected/rebated to customers over the 2012 to 2016 period based on the clearance of the deferral and variance accounts (discussed in the next section), the disposition of the smart meter costs, the disposition of the stranded meter costs and the clearance of the PP&E deferral account based on both the 20 year amortization proposal of HHH and the four year amortization proposal supported by Energy Probe. The data is taken from tables on pages 15 and 16 of the Partial Settlement Agreement dated February 29, 2012 for the smart and stranded meter cost recovery, from Table 9-7 of Exhibit 9, Tab 3, Schedule 1 for the other deferral and variance accounts and from the March 21, 2012 letter for the PP&E deferral account.

The table clearly shows that the HHH proposal results in larger increase in recovery from customers in 2012 than does the four year amortization supported by Energy Probe. Similarly, the reduction in the recovery in 2016, after all the accounts are cleared, with the exception of the PP&E deferral account under the HHH proposal, the reduction is larger under the HHH proposal. In other words, the rate volatility is larger in 2012 and 2016 under the HHH proposal, with no difference between the proposals in the 2013 to 2015 period.

<b><u>Deferral &amp; Variance Account Recovery</u></b>					
	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
<b><u>HHH Proposal</u></b>					
PP&E Deferral Account	(92,415)	(92,415)	(92,415)	(92,415)	(82,040)
Other D & V Accounts	313,970	313,970	0	0	0
Smart Meters	320,644	320,644	320,644	320,644	0
Stranded Meters	<u>283,002</u>	<u>283,002</u>	<u>283,002</u>	<u>283,002</u>	<u>0</u>
Total	825,201	825,201	511,231	511,231	(82,040)
Change in Recovery	825,201	0	(313,970)	0	(593,271)
<b><u>Four Year Amortization Proposal</u></b>					
PP&E Deferral Account	(261,056)	(261,056)	(261,056)	(261,056)	0
Other D & V Accounts	313,970	313,970	0	0	0
Smart Meters	320,644	320,644	320,644	320,644	0
Stranded Meters	<u>283,002</u>	<u>283,002</u>	<u>283,002</u>	<u>283,002</u>	<u>0</u>
Total	656,560	656,560	342,590	342,590	0
Change in Recovery	656,560	0	(313,970)	0	(342,590)

Energy Probe also notes that the increase in rates under the HHH proposal is significant in 2012. As shown in the Revenue Requirement Work Form included in Appendix K to the Partial Settlement Agreement, the base revenue requirement for HHH is \$9,411,657. This figure has been further reduced as a result of the cost of capital parameters issued by the Board on March 2.

The \$825,201 that would be recovered for the various deferral and variance accounts under the HHH proposal represents an increase to the base revenue requirement of 8.8%, and an even higher percentage of the base revenue requirement that reflects the cost of capital parameter update. The corresponding figure based on the \$656,560 that results from the four year amortization supported by Energy Probe is 7.0%. Both figures represent a substantial add on to the base revenue requirement that will be recovered from customers.

Energy Probe submits that the significant cash flow impacts on HHH, which is the third reason given in support of their proposal, is not credible.

The four year amortization period supported by Energy Probe results in a reduction to customers of \$261,056. Even if one ignores the fact that:

- (a) \$51,876 of this is related to a return on an investment that exists only because of the change from CGAAP to MIFRS and is not the result of any additional investment by the utility; and,
- (b) that the utility is recovering additional depreciation expense as part of the revenue requirement as a result of the increase in the gross asset values, again related to MIFRS and not to additional capital spending,

Energy Probe submits that the cash flow impacts of a reduction of \$261,056 are not significant for a utility the size of HHH. The annual amount equates to an amount of about \$21,750 per month.

To put this amount into perspective, the average monthly compensation costs for HHH for benefits (excluding salary & wages) for management only, based on the figures provided in Exhibit 4, Tab 2, Schedule 6, Table 4-16 for the test year is about \$22,900 per month. In other words, the cash flow impact is less than the cost of management benefits on a monthly basis.

Further, as demonstrated in the table provided above, the cash flow impact of all of the deferral and variance accounts, including smart and stranded meter costs, is a positive cash flow of nearly \$2 million over the 2012 through 2015 period.

Based on the above analysis, Energy Probe submits that the Board should reject the HHH proposal for a 20 year amortization period and direct HHH to use a four year period. The HHH proposal increases intergenerational inequity relative to a four year amortization period and it increases rate volatility relative to a four year amortization. There is no significant cash flow impact on the utility of using the four year amortization period.

## **D - DEFERRAL AND VARIANCE ACCOUNT CLEARANCE**

Energy Probe does not have any issues with the amounts in the deferral and variance accounts that HHH is proposing to clear as part of this proceeding. HHH proposes to recover these balances from ratepayers over two years.

If the Board determines that HHH should amortize the PP&E deferral account over four years, then Energy Probe accepts the 2 year account clearance as being reasonable.

If, however, the Board determines that HHH should be allowed to amortize the PP&E deferral account over 20 years, then Energy Probe submits that the clearance of deferral and variance accounts should be extended from 2 to 4 years. This has the impact of smoothing the amounts to be recovered from the various accounts and reduce rate volatility. It would also be consistent with the length of recovery associated with the smart and stranded meter costs.

## **E - LONG-TERM DEBT RATE**

Energy Probe submits that HHH has overestimated the appropriate long-term debt rate that should be used to calculate the long-term debt component of the revenue requirement.

HHH's evidence at Exhibit 5, Tab 1, Schedule 3 shows only one debt instrument used in the calculation of the long-term debt rate for the 2012 test year. This is the Promissory Note from the affiliate Town of Halton Hills in the amount of \$16,141,970. This debt instrument is described at Exhibit 5, Tab 1, Schedule 1, page 2. No other debt instruments are described in the evidence. Energy Probe has no issues with the application of the 4.41% to this loan agreement based on the Board's March 2, 2012 letter on the cost of capital parameter updates for 2012 cost of service applications for rates effective May 1, 2012. The debt instrument is with an affiliate and is at a variable rate (Tr. Vol. 1, page 45).

Through the interrogatory, technical conference and hearing process, two other debt instruments were determined to be used for 2012. Energy Probe deals with each of these below.

### **i) 2012 Capital Financing Loan**

In the EB-2009-0084 Report of the Board on the Cost of Capital for Ontario's Regulated Utilities dated December 11, 2009, the Board stated, at page 53 that:

*"the onus is on the distributor that is making an application for rates to document the actual amount and cost of embedded long-term debt and, in a forward test year, forecast the amount and cost of new long-term debt to be obtained during the test year to support the reasonableness of the respective debt rates and terms."*



HHH has indicated that it will need to borrow \$5 million to finance its 2012 capital expenditures (Energy Probe Interrogatory #62). When asked why HHH did not include this new debt in its forecasted cost of long-term debt, Mr. Skidmore indicated that it was an oversight (Tr. Vol. 1, pp. 38-39). Energy Probe agrees with HHH that this loan should be included in the calculation of the long-term cost rate. Energy Probe also agrees that the amount of \$5 million is a reasonable estimate of the financing required for the 2012 capital expenditures.

The \$5 million will be drawn down in tranches (Technical Conference Tr. Vol. 1, page 7). Mr. Skidmore confirmed that HHH will be drawing on this loan as they make the capital expenditures through 2012 (Tr. Vol. 1, page 39). Based on this response, Energy Probe submits that the average amount to be included in the calculation of the long-term debt is one-half of the amount forecast to be borrowed, or \$2.5 million. This figure matches with the result of the methodology that incorporates the capital expenditures into rate base, being the average of the opening and closing balances.

With respect to the rate (and the corresponding term), Energy Probe submits that HHH has failed to meet its onus to forecast the cost of new long-term debt.

In this absence, Energy Probe submits that the Board should determine a rate and term based on the most recent evidence before it. In particular, HHH has two loan agreements currently in place. One is with an affiliate with a term of 5 years (Board Staff Interrogatory #35, Appendix OEB 1-B). The other is for a term of 1 year for the smart meters discussed in the previous section. As a result, Energy Probe submits it is reasonable to expect that HHH will have a 5 year term on the \$5 million loan, given the lack of any loan agreements in excess of this length of duration.

In the response to Energy Probe Interrogatory #62(a), HHH indicated that they were quoted a rate of 3.20% from the TD Commercial Bank for a 5 year term loan. In the response to School Energy Coalition Interrogatory #27, HHH indicated that its financial institution provided a lower rate and more flexible terms than it could receive from Infrastructure Ontario.

Mr. Skidmore confirmed that HHH could still obtain funding from its financial institution (Td Commercial Bank) at a lower rate and with more flexible terms than it could get from Infrastructure Ontario (Tr. Vol. 1, pp. 43-44). Energy Probe notes that HHH has updated the record in this proceeding in its Argument-in-Chief where, in paragraph 30, it is indicated that the current rate available for a 5 year term from Infrastructure Ontario is 2.52%.

Given that that the most recent rate on the record of this proceeding for a 5 year term loan from Infrastructure Ontario is 2.52% and that HHH has confirmed that it can still get a lower rate from TD Commercial Bank, Energy Probe submits that the rate of 2.52% should be the ceiling on the rate used for this loan in the calculation of the overall long-term debt cost.

## **ii) Smart Meter Loan**

HHH has a loan from TD Commercial Bank in the amount of \$3,943,430 (Energy Probe Technical Conference Question #6) with a term of one year at a rate of 2.13%. The one year term expires in August, 2012 (Technical Conference Tr. Vol. 1, page 7).

Mr. Smelsky indicated at the technical conference that it was unknown what the term of the replacement loan would be, or what the rates would be (Technical Conference Tr. Vol. 1, page 7). Mr. Smelsky indicated the \$3.943 million loan was part of the third credit facility that was provided in Appendix SEC 1-C to School Energy Coalition Interrogatory #13 (Tr. Vol. 1, pp. 34-35). This third credit facility is a Committed Term Facility available at the borrowers option. This loan is described as a floating rate term loan available by way of a prime rate based loan or a bankers acceptance.

When asked if HHH had a better forecast than it did at the technical conference of what it intended to do to replace this loan for the \$3.9 million when it came due in August, 2012, Mr. Smelsky indicated that they did not (Tr. Vol. 1, pp. 35-36). When pressed for any further information on the replacement for this loan, Mr. Skidmore stated that "*It will be known at the time that we would renew the loan.*" (Tr. Vol. 1, page 36). Energy Probe submits that HHH has again failed to meet its onus to forecast the cost of new long-term debt that will replace the existing debt and has left a vacuum in the evidence.

Energy Probe submits that this vacuum should be filled based on the following evidence. The rate for the January through August, 2012 period is 2.13%, as stated in the response to Energy Probe Technical Conference Question #6(a). Therefore there is a need to estimate the rate for the last four months of 2012 to come up with a weighted average rate for this loan.

As noted in the loan agreement in Appendix SEC 1-C of the response to School Energy Coalition Interrogatory #13, the rate applicable to the third credit facility, the Committed Term Facility, is based on the prime rate + 0.00% per annum if it is a prime based loan or the stamping fee + 1.40% if it is a bankers acceptance.

Energy Probe submits that the simplest approach is to assume that a prime based loan would be continued for the last four months of 2012. The current prime rate at the TD Bank is 3.00%. This is a reasonable forecast to use for the last four months of 2012.

Based on the 3.00% for four months and the 2.13% that is in place for the first eight months of the year, the weighted average rate that should be applied to the principal of \$3,943,430 would be 2.42%. Energy Probe notes that this rate is very comparable to the 2.52% ceiling on what HHH has indicated it can borrow the \$5 million from the TD Commercial Bank to finance its 2012 capital expenditures.

HHH has indicated that it did not include this loan in the calculation of the overall long-term debt rate because they do not consider it as part of the long-term debt because it is on a one year renewal (Tr. Vol. 1, page 37).

The question for the Board to consider is whether or not a one year term loan should be considered a long-term debt instrument. Energy Probe submits that the appropriate response in this instance is yes and that the Board should direct HHH to include this loan in the calculation of its overall long-term debt rate for two compelling reasons.

First, and most importantly, this term loan is being used to finance specific long-term assets. Specifically, it is being used to finance smart meters. There is no dispute about this point. The loan agreement referenced above states that the Committed Term Facility is to be used to take out the Facility #2 in the loan agreement. Facility #2 was to "*finance smart meter implementation (hardware and installation)*". Mr. Smelsky agreed that the \$3.9 million was used to finance the smart meter investment (Tr. Vol. 1, page 35).

Second, the agreement with TD Commercial Bank is a multi-year agreement entered into in December 2009. The agreement consists of three types of credit and borrowing options: an operating loan, an interim demand loan and the aforementioned committed term facility, which was to be used to take out the interim demand loan that was used to finance the smart meter assets. In other words, the one year committed term facility was the last year of a multi-year loan agreement to finance smart meters.

If the Board determines that the smart meter loan that exists through to August 2012 should not be part of the long-term debt calculation, Energy Probe submits that the replacement loan for the smart meters should be considered long-term debt since HHH should match the life of its assets with the life of the financing for those assets. This debt would then be considered long-term and would be in place for 4 months in the test year and should be factored into the calculation of the overall long-term debt rate at the same rate as for the 2012 capital financing loan.

### **iii) Long-Term Debt Rate**

Based on the rate of 4.41% for the affiliate loan and the submissions on the appropriate rates and amounts related to the Smart Meter Loan and the 2012 Capital Financing Loan, Energy Probe submits that the overall long-term debt rate should be 3.85%, as calculated in the following table. This rate reflects appropriate rates for the three different loans that underpin long-term assets, and it also reflects an appropriate approach to calculate the average principal outstanding during the test year.

<b><u>Cost of Long-Term Debt</u></b>					
	Opening	Closing	Average		Interest
<u>Debt Holder</u>	<u>Principal</u>	<u>Principal</u>	<u>Principal</u>	<u>Rate</u>	<u>Cost</u>
Town of Halton Hills	16,141,970	16,141,970	16,141,970	4.41%	711,861
TD Commercial Bank (1)	3,943,430	3,943,430	3,943,430	2.42%	95,431
TD Commercial Bank	0	5,000,000	2,500,000	2.52%	63,000
Total	20,085,400	25,085,400	22,585,400		870,292
Weighted Average Cost					3.85%

## **F - OM&A COSTS**

### **i ) Overall Increase (CGAAP)**

HHH is requesting the approval of a significant increase in OM&A costs in the 2012 test year as compared to the actual OM&A expenditures in 2009 through 2011. The following table shows the actual OM&A expenditures for 2008 through 2011 on a CGAAP basis and the 2012 request, also on a CGAAP basis. This information has been compiled from a number of sources, including Board Staff Interrogatory #23, Energy Probe Interrogatory #37, Undertaking JT1.10 and the Partial Settlement Agreement.

<b><u>OM&amp;A Expenditures</u></b>					
	Actual	Actual	Actual	Actual	Forecast
	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
OM&A Expenditures	5,167,120	4,515,477	4,475,435	4,646,940	5,987,400
Change (%)		-12.6%	-0.9%	3.8%	28.8%

When viewed as a change from the 2008 expenditure of \$5,167,120, the increase to 2012 does not look out of line, at a compounded annual growth rate of about 3.75% per year. However, in Energy Probe's view this is not an appropriate comparison. Neither is a comparison to the Board Approved figure in the 2008 cost of service application of \$5,124,000 (Exhibit 4, Tab 1, Schedule 1, Table 4-1). To start the comparison with either of these 2008 figures ignores what HHH has been able to accomplish under the incentive rate making ("IRM") mechanism.

HHH explained the reduction in the 2009 OM&A expenses as compared to those in 2008 based on three major changes. These changes are summarized in Table EP 2-12 provided in the response to Energy Probe Interrogatory #68 and were discussed during the oral hearing (Tr. Vol. 1, pp. 62-64). The changes were related to more capital work and the resulting increase in capitalized labour, the replacement of contract service work by an in-house engineer and organizational changes. Mr. Skidmore indicated that the restructuring took place in the 2009 through 2010 period, with no staff hired until 2011 (Tr. Vol. 1, page 77). This is reflected in the total number of employees shown in Table 4-16 of Exhibit 4, Tab 2, Schedule 6.

OM&A costs in 2010 and 2011 are at similar levels to recorded in 2009. The 2011 figure is approximately 3% higher than the 2009 cost, but still more than \$500,000 or 10% below the actual 2008 expenditures.

HHH indicated that it was not lacking in any standard utility practices over the 2008 though 2011 IRM period, nor did HHH forego any basic needs of the utility over this period (Tr. Vol. 1, page 77).

In its Argument-in-Chief, HHH provides an analysis in Table 1 to justify their requested OM&A that begins with the Board approved OM&A from the 2008 cost of service application. Energy Probe submits that this starting point is not appropriate. It does not reflect the more recent actual expenditures that the utility has achieved and maintained as a result of increased capitalization due to higher capital expenditures, the savings from doing more work in-house and the efficiencies gained from the structural organizational changes.

The evidence clearly indicates that these changes that decreased costs in 2009 relative to 2008 and which HHH has been able to maintain in 2010 and 2011 are sustainable into 2012.

In particular, the reduction in OM&A due to higher capitalization linked to higher capital expenditures is sustainable because HHH has indicated that it will be doing more capital work in 2012 than in previous years (Tr. Vol. 1, page 65); the savings from doing more work in-house will continue as HHH is not proposing to contract this work out in 2012; and there is no evidence that HHH is going to reverse or somehow change the organizational changes that have taken place in 2009 and 2010 that would increase cost substantially in 2012. In relation to this last point, Mr. Skidmore indicated that one of the reasons that the average management salary has declined in 2012 is because of the flattened organizational structure that was implemented resulting in less senior executives and less supervisors (Tr. Vol. 1, page 67).

HHH has not provided any evidence that its service quality metrics have declined over the 2008 through 2011 period. This is also reflected in Mr. Skidmore's statement, noted earlier, that HHH has not been lacking in any standard utility practices.

Energy Probe submits that the substantial increase in the forecasted 2012 OM&A expenses after the sustainable levels recorded in 2009 through 2012 should not be approved by the Board. To do so reflects poorly on the entire IRM rate setting methodology. A utility can spend substantially less than the amount for the base year as approved by the Board without having to share any of those savings with ratepayers. The entire benefit accrues to the shareholder. Then, upon rebasing, the OM&A costs increase materially and all of the efficiency and productivity gains that are evident during the IRM period miraculously disappear and ratepayers do not benefit from any of the historical gains achieved on a going forward basis.

Energy Probe submits that the Board should approve a CGAAP based OM&A amount for the 2012 test year for HHH in the range of \$5.25 to \$5.5 million. Energy Probe has arrived at this range based on the foregoing analysis of the sustained lower costs incurred in 2009 through 2011, along with previous Board decisions related to OM&A. In particular, in the EB-2009-0259 (Burlington Hydro Inc.) and EB-2010-0132 (Hydro One Brampton Networks Inc. - "Brampton") decisions, the Board approved an increase in the test year OM&A of 10% over the last historical year. In both cases, bridge year actual data was not available.

In particular, in the EB-2010-0132 Decision and Order dated April 4, 2011, after making a number of adjustments to the OM&A forecast (for 2011) the Board noted at page 23:

*"... that the remaining OM&A is approximately 16% higher than 2009 actual spending, an average of approximately 8% per annum. Given the relatively modest growth in customers forecast for the test period, and the relatively*

*modest rate of inflation, and the lack of any compelling evidence why a large increase is warranted, the Board finds this increase to be excessive. The Board finds that an increase of 10% over 2009 actual spending is reasonable. Given the 2.2% per annum forecast growth in customers, this allows for slightly less than 3% per annum increase in spending per customer, which is more than the rate of inflation."*

Energy Probe submits that the circumstances that existed at the time of the Brampton decision still exist today. The rate of inflation is still relatively modest. The customer growth for HHH, a utility in close proximity to Brampton, is 2.2% in 2012, following an increase of 0.8% in 2011 (Appendix D to Partial Settlement Agreement). The increase in 2012 for HHH is the same as the increase forecast for Brampton, while the increase in the bridge year is lower than that for Brampton.

Energy Probe submits that the Board should apply the same reasoning to the increase in OM&A costs for HHH as it did for Brampton. In particular, Energy Probe submits that an increase of 10% over actual 2010 expenditures is appropriate as a starting point. Based on the 2010 CGAAP expenditures of \$4,475,435, this would result in a base for 2012 of \$4,922,978. Energy Probe notes that 2011 preliminary data is available for HHH and the Board could consider adding 5% to the \$4,646,940. This would result in a 2012 base of \$4,879,287, a figure lower than that proposed by Energy Probe.

On top of the 2012 base proposed by Energy Probe, it is submitted that the incremental costs related to the smart meters of \$327,710 (Argument-in-Chief, Table 3) should be added on as these incremental costs were not part of the OM&A expense recorded in 2010. The addition of this cost would result in a figure of \$5,250,688.

Energy Probe submits that this is the bottom of a reasonable level of OM&A for 2012 calculated on a CGAAP basis. This increase provides for growth in compensation and/or headcount, along with cost changes for purchased services and other OM&A costs.

The one item that Energy Probe submits that there may be merit in treating outside of this envelope is the increase in tree trimming expenses of \$250,000 in the 2012 test year (Tr. Vol. 1, page 72).

As shown in the response to Undertaking J1.6, the tree trimming expense was \$109,000 in 2008, dropping to \$77,000 in 2009 before increasing to \$120,000 in 2010.

In 2011 the tree trimming expense appears to be about \$140,000. Table EP 2-12 provided in Energy Probe Interrogatory #68 indicates that the 2012 request is \$250,000 above the 2010 level, which, as shown in Undertaking J1.6 was approximately \$120,000.

This results in a 2012 request for tree trimming of \$370,000 and since the 2012 request is shown as being \$230,000 above the 2011 level in Table EP 2-12, this results in the 2011 forecast of \$140,000 noted above.

The significant increase forecast for 2012 is based on the high tree growth rate, excessive disease and die back of mature trees in recent years, as stated in the non-confidential description of the document that was requested to be kept confidential that was attached to the March 12, 2012 from Norton Rose on behalf of HHH.

Energy Probe submits that the need for tree trimming is not an activity that should require a significant change from one year to the next. In this proceeding, HHH is asking the Board to approve a 264% increase between 2011 and 2012 in this expense. The increase is more than 300% when 2010 is used as the starting point. Tree growth rates and die back rates may vary from year to year reflecting impacts of wind storms, cold winters or periods of drought, but the impact of these changes can be seen.

The non-confidential description to the March 12, 2012 letter indicated that Mr. Lang, a certified arborist, concluded that HHH's line clearance program had been underfunded for a significant number of years and that tree encroachment issues were prevalent throughout much of HHH's system. However, at the same time, Mr. Skidmore testified (Tr. Vol. 1, page 77) that HHH was not lacking in any standard utility practices over the 2008 through 2011 period. Further, Mr. Skidmore indicated that the change in tree trimming was not a fundamental change in approach (Tr. Vol. 1, page 82).

Energy Probe submits that there appears to be a contradiction in the evidence regarding tree trimming. HHH submits that the significant increase in costs for which it is seeking recovery in the test year is not the result of any lack of standard utility practice and that the change proposed is not a fundamental change. On the other hand, a report from an independent third party, which is the only evidence that HHH is relying on in support of the increase, states that the tree trimming budget has been under-funded for a significant number of years.

Energy Probe notes that over several of these years (2009 through 2011) where the tree trimming budget has been under-funded, HHH spent considerably less in total OM&A costs that were approved by the Board in 2008 rates.

In other words, the shareholder of HHH benefitted directly from the under-funding of the tree trimming budget in those years. Now, under cost of service, ratepayers are being asked to pay the full burden for the shortfalls in the previous year without the shareholder taking any responsibility for the problem.



Energy Probe likens this situation to that of a teenager (shareholder) asking to borrow the car and asking his parents (ratepayers) to give him \$20 for gas. Later in the evening the parents get a phone call from the teenager saying he ran out of gas and now needs \$40 to have his car towed to the gas station. After finding out that the teenager spent the \$20 on pizza rather than gasoline, the parents may well tell the teenager that he is the cause of his own problem and that he is responsible for the towing charges.

If the Board accepts the need for the entire incremental tree trimming cost increase of \$250,000 based on the third party report, and that the entire increase should be paid for by ratepayers with no responsibility attributed to the shareholder for past decisions, then the total OM&A figure proposed by Energy Probe on a CGAAP basis inclusive of the incremental smart meter costs would be approximately \$5.5 million.

#### **ii) Increase Due to MIFRS**

The increase in the forecasted 2012 OM&A budget due to the conversion from CGAAP to MIFRS has been estimated by HHH to be \$286,621 (Energy Probe Interrogatory #35). Energy Probe believes this estimate is reasonable and should be accepted by the Board.

#### **iii) Specific Adjustments to OM&A**

Energy Probe would normally provide an analysis of specific reductions to OM&A expenses that would approximate the overall reduction in OM&A expenditures proposed above. However, except for the specific adjustments noted below, this is not possible in this proceeding.

It became apparent throughout the proceeding that costs in specific accounts could not be compared to historical levels because of the reallocation of amounts between different accounts in different years (Tr. Vol. 1, pp. 71-77).

Despite this problem of comparing cost increases across the years by account, Energy Probe has been able to provide submissions in a number of areas, as discussed below.

First, the total employee costs charged to OM&A is a significant contributor to the overall increase in OM&A costs. The following table shows the total employee costs for 2008 through 2012 broken down between the costs charged to OM&A and capital. This information is taken directly from Table 4-16 in Exhibit 4, Tab 2, Schedule 6.

<b>Total Employee Costs</b>					
	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
Charged to OM&A	3,326,721	2,836,303	3,127,045	3,156,076	3,689,022
Charged to Capital	832,540	1,023,666	967,602	1,203,143	1,416,806
Total Employee Costs	4,159,261	3,859,969	4,094,647	4,359,219	5,105,828
% Change		-7.20%	6.08%	6.46%	17.13%

The 2009 decrease in total employee costs reflects the organizational changes that took place at HHH. The increases of 6.1% and 6.5% in 2010 and 2011, respectively, reflect both changes in FTE's and change in compensation. The increase in 2012 of 17.1% is substantially above the increases shown for 2010 and 2011.

Energy Probe also notes that the employee costs charged to OM&A of \$3,689,022 as shown in the above table represents nearly 60% of the \$6,274,021 (including MIFRS) being requested by HHH.

Energy Probe submits that inflation for 2012 is virtually the same as that experienced in 2010 and 2011. Energy Probe further submits that HHH has not justified an increase of 4 FTE's as forecast in Table 4-16 between 2011 and 2012 or the increase of 7 positions above the level of 44 shown in both 2009 and 2010.

In the EB-2011-0273 Decision and Order for Grimsby Power Inc. dated January 16, 2012, the Board approved an increase in OM&A expenditures in the 2012 test year of approximately 26% over the 2010 actual expenditures. A significant part of this increase was related to the addition of two staff members (increasing from 17 FTEs in 2010 to 19 in 2012). The Board found that there was compelling evidence to justify the significant increase in OM&A costs. In particular, the Board stated (page 9) that:

*"Grimsby has proven its case for the increase in staff and additional funds to enable the utility to operate in a sustainable manner and to adopt standard utility practices, which were found to be previously lacking." and that "The Board accepts that a resetting of OM&A expenses for 2012 is appropriate in order to bring Grimsby's operations, maintenance and administration practices closer to the established basic practices of other utilities."*

In the Grimsby proceeding, the Board found that standard utility practices had been lacking over the IRM term. Energy Probe submits that this is not the case for HHH. Mr. Skidmore confirmed this when he indicated that HHH has not lacked in any standard utility practices (Tr. Vol. 1, page 77). Energy Probe submits that HHH has not justified the need for an increase in FTEs between the 2010 to 2012 from 44 to 51, an increase of 16%. The Grimsby increase from 17 to 19 over the same period is an increase of only 12%.

Energy Probe submits that total employee costs for 2012 should be allowed to increase for rate setting purposes at the same rate as they did in 2010 and 2011. As shown in the above table, the average increase in total compensation costs over this period was 6.27%. Applying this increase to the 2011 figure results in total employee costs of \$4,632,542 for the test year. Applying the same capitalization rate as reflected in the above table results in the amount of total employee costs capitalized to OM&A of \$3,347,067, a reduction of \$342,000. Energy Probe submits this is a reasonable reduction to the 2012 OM&A expenses.

Second, HHH has forecast an increase of \$63,000 related to Account 5630, Outside Services Employed between 2011 and 2012 as shown in Table EP 1-32 provided in the response to Energy Probe Interrogatory #35. This increase was related to costs related to actuarial calculations needed for post-employment benefit calculations and contract negotiations that will be near the end of 2012 (Tr. Vol. 1, page 76). Energy Probe submits that these are not annual costs and should be amortized over the 4 year IRM term, resulting in a reduction in the costs from \$63,000 to \$15,750, for a reduction of \$47,250.

Third, HHH has not provided any justification for the \$57,606 increase in OM&A in 2012 from 2011 shown in Table EP 2-12 in Energy Probe Interrogatory #68. This increase, noted as a variance relating to changes in allocation methodologies and cost drivers in 2009 and 2010, reverses a trend that is reflected in lower OM&A costs in 2009 through 2011 resulted in 2011 OM&A expenses being reduced by approximately \$400,000. This reduction was attributable to the increase in capital work being done over this period (Tr. Vol. 1, pp. 62-63). Energy Probe submits that HHH has not provided any credible evidence to support the reversal of this trend. In fact, HHH indicated that the amount of capital work was forecast to increase for 2012. This should support the continuation of the trend of higher capitalized OM&A expenditures and lower employee costs charged to OM&A, not reverse the trend.

Fourth, as noted earlier under the submissions related to the Green Energy Initiative, Energy Probe does not support the inclusion of these expenditures in the revenue requirement. This would reduce the OM&A expenses by \$11,760 (Partial Settlement Agreement, page 12).

Fifth, as shown in Table EP 1-32 in Energy Probe Interrogatory #35, HHH is forecasting an increase in Account 5620 Office Supplies and Expenses of more than \$20,000 between 2010 and 2012, following an increase of less than \$5,000 in 2010 and a decrease in 2009. Energy Probe submits that an increase of \$5,000 per year over the 2010 level

would result in a 2012 forecast of \$50,102, a reasonable estimate given the rate of inflation, customer growth and postal increases over this period. This results in a reduction of OM&A costs in the test year of \$10,750.

Finally, Energy Probe submits that the property tax forecast should be reduced by \$8,000. As shown in Table EP 1-35 in the response to Energy Probe Interrogatory #37, the increase in property taxes between 2011 and 2008 on an actual basis has been about 1.7% per year. Applying this growth rate to the 2011 actual expense of \$96,839 results in a 2012 forecast of approximately \$98,500 in place of the \$106,600 included in the forecast.

In summary, Energy Probe has identified specific adjustments that total approximately \$477,366 (\$342,000 in total employee costs charged to OM&A; \$47,250 related to amortizing outside costs that are not incurred on annual basis; \$57,606 related to the reversal of capitalizing more employee costs; \$11,760 related the removal of the GEI; \$10,750 related to office supplies and expenses; \$8,000 for property taxes). This amount is comparable to the reduction of \$487,400 that would result from the \$5.5 million noted as the upper bound of the range proposed by Energy Probe on an envelope basis.

## **G - COSTS**

Energy Probe requests that it be awarded 100% of its reasonably incurred costs. Energy Probe has attempted to minimize its time on this application, while at the same time ensuring a thorough review. This has been accomplished through cooperation with other intervenors to ensure no significant overlaps took place throughout the regulatory process.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

**April 13, 2012**

**Randy Aiken**

**Consultant to Energy Probe**

## APPENDIX A

Halton Hills Hydro Inc.  
Revised Table EP TC-1 reflecting OM&A, Updated Cost of Capital  
and CCA as proposed by HHH

Capital Expenditure	1,400,000
Depreciation Expense	35,000
Net Book Value	1,365,000
OM&A	11,760
Fixed Assets Opening Balance 2012	-
Fixed Assets Closing Balance 2012	1,365,000
<b>Average Fixed Asset Balance for 2012</b>	682,500
Working Capital Allowance	1,764
<b>Rate Base</b>	684,264
Regulated Rate of Return	6.20%
<b>Regulated Return on Capital</b>	42,424
Deemed Interest Expense	17,466
Deemed Return on Equity	24,959
OM&A	11,760
Regulated Return on Capital	42,424
Depreciation Expense	35,000
	89,184
Pils	726
<b>Revenue Requirement</b>	<b>89,911</b>
<b>Pils:</b>	
CCA	56,000
(1,400,000 x 8% x 50%)	
Deemed Return on Equity	24,959
Add Depreciation	35,000
Less CCA	(56,000)
	3,959
Pils before Gross Up	614
Grossed Up - Pils	726

**APPENDIX B**

Halton Hills Hydro Inc.

Net Present Value of Green Energy Initiative  
with CCA as Proposed by HHH

Net Present Value of Green Energy Initiative with CCA as Proposed by HHH		Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15	Year 16	Year 17	Year 18	Year 19	Year 20	Year 21	
Capital Expenditure	1,400,000	1,365,000	1,295,000	1,225,000	1,155,000	1,085,000	1,015,000	945,000	875,000	805,000	735,000	665,000	595,000	525,000	455,000	385,000	315,000	245,000	175,000	105,000	35,000	
Depreciation Expense	35,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	35,000	
Net Book Value	1,365,000	1,295,000	1,225,000	1,155,000	1,085,000	1,015,000	945,000	875,000	805,000	735,000	665,000	595,000	525,000	455,000	385,000	315,000	245,000	175,000	105,000	35,000	-	
OM&A	2.50% 11,760	12,054	12,355	12,664	12,981	13,305	13,638	13,979	14,328	14,687	15,054	15,430	15,816	16,211	16,617	17,032	17,458	17,894	18,342	18,800	19,270	
Deferral Account Offset - Cost of Power	(35,495)	(35,495)	(36,382)	(37,292)	(38,224)	(39,180)	(40,159)	(41,163)	(42,192)	(43,247)	(44,328)	(45,437)	(46,573)	(47,737)	(48,930)	(50,154)	(51,407)	(52,693)	(54,010)	(55,360)	(56,744)	
Fixed Assets Opening Balance	-	-	-	-	1,155,000	1,155,000	1,155,000	1,155,000	875,000	875,000	875,000	875,000	595,000	595,000	595,000	595,000	315,000	315,000	315,000	315,000	35,000	
Fixed Assets Closing Balance	1,365,000	1,365,000	1,365,000	1,365,000	1,085,000	1,085,000	1,085,000	1,085,000	805,000	805,000	805,000	805,000	525,000	525,000	525,000	525,000	245,000	245,000	245,000	245,000	-	
Average Fixed Asset Balance	682,500	682,500	682,500	682,500	1,120,000	1,120,000	1,120,000	1,120,000	840,000	840,000	840,000	840,000	560,000	560,000	560,000	560,000	280,000	280,000	280,000	280,000	17,500	
Working Capital Allowance	1,764	1,764	1,764	1,764	1,947	1,947	1,947	1,947	2,149	2,149	2,149	2,149	2,372	2,372	2,372	2,372	2,619	2,619	2,619	2,619	2,891	
Rate Base	684,264	684,264	684,264	684,264	1,121,947	1,121,947	1,121,947	1,121,947	842,149	842,149	842,149	842,149	562,372	562,372	562,372	562,372	282,619	282,619	282,619	282,619	20,391	
Regulated Rate of Return	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	6.20%	
Regulated Return on Capital	42,424	42,424	42,424	42,424	69,561	69,561	69,561	69,561	52,213	52,213	52,213	52,213	34,867	34,867	34,867	34,867	17,522	17,522	17,522	17,522	1,264	
Deemed Interest Expense	17,466	17,466	17,466	17,466	28,638	28,638	28,638	28,638	21,496	21,496	21,496	21,496	14,355	14,355	14,355	14,355	7,214	7,214	7,214	7,214	520	
Deemed Return on Equity	24,958	24,958	24,958	24,958	40,923	40,923	40,923	40,923	30,717	30,717	30,717	30,717	20,512	20,512	20,512	20,512	10,308	10,308	10,308	10,308	744	
OM&A	11,760	11,760	11,760	11,760	12,981	12,981	12,981	12,981	14,328	14,328	14,328	14,328	15,816	15,816	15,816	15,816	17,458	17,458	17,458	17,458	19,270	
Deferral Account Offset - Cost of Power	(35,495)	(35,495)	(35,495)	(35,495)	(38,224)	(38,224)	(38,224)	(38,224)	(42,192)	(42,192)	(42,192)	(42,192)	(46,573)	(46,573)	(46,573)	(46,573)	(51,407)	(51,407)	(51,407)	(51,407)	(56,744)	
Regulated Return on Capital	42,424	42,424	42,424	42,424	69,561	69,561	69,561	69,561	52,213	52,213	52,213	52,213	34,867	34,867	34,867	34,867	17,522	17,522	17,522	17,522	1,264	
Depreciation Expense	35,000	35,000	35,000	35,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	35,000	
	53,689	53,689	53,689	53,689	114,317	114,317	114,317	114,317	94,349	94,349	94,349	94,349	74,110	74,110	74,110	74,110	53,573	53,573	53,573	53,573	(1,210)	
Pils	726	726	726	726	4,989	4,989	4,989	4,989	7,473	7,473	7,473	7,473	8,721	8,721	8,721	8,721	9,085	9,085	9,085	9,085	2,511	
Revenue Requirement	54,415	54,415	54,415	54,415	119,306	119,306	119,306	119,306	101,822	101,822	101,822	101,822	82,831	82,831	82,831	82,831	62,657	62,657	62,657	62,657	1,302	
Pils:																						
CCA - accelerated 50.0%	(1,400,000 x 8% x 50%)	56,000	107,520	98,918	91,005	83,725	77,027	70,864	65,195	59,980	55,181	50,767	46,705	42,969	39,531	36,369	33,459	30,783	28,320	26,054	23,970	22,053
Accum. CCA			163,520	262,438	353,443	437,168	514,194	585,059	650,254	710,234	765,415	816,182	862,887	905,856	945,388	981,757	1,015,216	1,045,999	1,074,319	1,100,374	1,124,344	1,146,396
Deemed Return on Equity	24,958	24,958	24,958	24,958	40,923	40,923	40,923	40,923	30,717	30,717	30,717	30,717	20,512	20,512	20,512	20,512	10,308	10,308	10,308	10,308	744	
Add Depreciation	35,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	35,000	
Less CCA -accelerated 50.0%	(56,000)	(107,520)	(98,918)	(91,005)	(83,725)	(77,027)	(70,864)	(65,195)	(59,980)	(55,181)	(50,767)	(46,705)	(42,969)	(39,531)	(36,369)	(33,459)	(30,783)	(28,320)	(26,054)	(23,970)	(22,053)	
	3,958	(12,562)	(3,960)	3,953	27,198	33,896	40,058	45,727	40,737	45,536	49,950	54,012	47,543	50,981	54,143	57,053	49,526	51,988	54,254	56,338	13,691	
Pils before Gross Up	614	614	614	614	4,216	4,216	4,216	4,216	6,314	6,314	6,314	6,314	7,369	7,369	7,369	7,369	7,676	7,676	7,676	7,676	2,122	
Grossed Up - Pils	\$ 726	\$ 726	\$ 726	\$ 726	\$ 4,989	\$ 4,989	\$ 4,989	\$ 4,989	\$ 7,473	\$ 7,473	\$ 7,473	\$ 7,473	\$ 8,721	\$ 8,721	\$ 8,721	\$ 8,721	\$ 9,085	\$ 9,085	\$ 9,085	\$ 9,085	\$ 2,511	

Discount Rate	6.20%
Capital Cost of Project	\$ 1,400,000
Revenue in Year 1	\$ 54,415
Present Value of Revenues from Year 2 to 21	\$ 954,483
Total Revenue	\$ 1,008,899
<b>Net Present Value</b>	<b>\$ (391,101)</b>