ONTARIO ENERGY BOARD

FILE NO.: **EB-2012-0161**

VOLUME: **1**

DATE: **October 29, 2012**

BEFORE: **Ken Quesnelle** Presiding Member

Marika Hare Member

EB-2012-0161

THE 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 PowerStream Inc. for an order approving just and reasonable rates and other charges for electricity distribution to be effective January 1, 2013.

Hearing held at 2300 Yonge Street,
25th Floor, Toronto, Ontario,
on Monday, October 29th, 2012,
commencing at 9:38 a.m.

VOLUME 1

BEFORE:

KEN QUESNELLE Presiding Member

MARIKA HARE Member

A P P E A R A N C E S

KRISTI SEBALJ	Board Counsel
MARTIN DAVIES	Board Staff
JAMES SIDLOFSKY	PowerStream Inc.
RANDY AIKEN	Energy Probe Research Foundation
JULIE GIRVAN ROBERT WARREN	Consumers Council of Canada (CCC)
JAY SHEPHERD DEB DEVGAN	School Energy Coalition (SEC)

INDEX OF PROCEEDINGS

E X H I B I T S

U N D E R T A K I N G S

Monday, October 29, 2012

--- On commencing at 9:38 a.m.

MR. QUESNELLE: Good morning. Please be seated.

The Board sets today on a matter of an application filed by PowerStream Incorporated on May 28th, 2012 under section 78 of the OEB Act. PowerStream is seeking approval for changes to the rates it charges for electricity distribution to be effective January 1, 2013.

The Board issued a Notice of Application and Hearing on June 7th, 2012 under file number EB-2012-0161. Since that date, the Board has accepted intervenors and issued procedural orders dealing with a confidentiality claim and the establishment of the schedule for interrogatories and responses, as well as the establishment of technical and settlement conferences.

These conferences have taken place, and as a result of the discussions at the settlement conference, a partial settlement has been reached between the intervening parties and PowerStream.

This date has been set aside for an oral hearing of all matters that require a hearing by the Board. We will start this morning by first receiving a presentation of the proposed partial settlement, and then we will consider our acceptance of it. Subject to our acceptance of the proposed partial settlement, it is our intention to then proceed and hear the unsettled issues.

I understand that PowerStream is prepared to present its witnesses on these matters this morning.

My name is Ken Quesnelle and with me on the Panel is Board Member Marika Hare.

I will now take appearances.

APPEARANCES:

MR. SIDLOFSKY: Good morning, sir. My name is James Sidlofsky, counsel to PowerStream with Borden Ladner Gervais.

MR. QUESNELLE: Mr. Sidlofsky.

MR. SHEPHERD: Good morning. My name is Jay Shepherd. With me is Deb Devgan for the School Energy Coalition.

MR. QUESNELLE: Mr. Shepherd.

MS. GIRVAN: Good morning. Julie Girvan for the Consumers Council of Canada, and I would like to enter an appearance for Robert Warren.

MR. QUESNELLE: Okay. Thank you, Ms. Girvan.

MS. SEBALJ: Ms. Sebalj for Staff, and with me, Martin Davies.

MR. QUESNELLE: Everyone's mics working properly this morning? I don't know if you caught all that.

MS. SEBALJ: Was I not close enough?

MR. QUESNELLE: Okay. All right. I think we have it all recorded anyway. Thank you very much.

Any preliminary matters before we get started with the presentation of the partial? Mr. Sidlofsky? Anyone else?

Okay. Mr. Sidlofsky, then, as we had suggested, we will take a brief presentation. I don't know if there's anything we'll -- if there are questions as we go through, Ms. Hare and I will pose them, but there is nothing that I would highlight in advance that we are particularly concerned of. A brief overview of the settled issues and the unsettled issues before we commence would be helpful.

MR. SIDLOFSKY: Thank you, sir. That is very helpful, and I actually said in my correspondence the other day that I would have very brief comments. So hopefully that is helpful to the Board too.

MR. QUESNELLE: Okay.

PRESENTATION OF SETTLEMENT AGREEMENT BY MR. SIDLOFSKY:

MR. SIDLOFSKY: PowerStream Inc. is the electricity distributor for 11 municipalities in York Region and Simcoe County; those include Markham, Vaughan, Barrie, Richmond Hill and Aurora.

PowerStream serves about 340,000 customers in those communities, making it the second-largest municipally owned distributor in Ontario.

PowerStream filed its 2013 forward test year cost of service distribution rate application with the Board in May of this year.

In its application, PowerStream sought approval to charge rates effective January 1st, 2013 to recover a service revenue requirement of approximately $179 million. After revenue offsets of approximately nine million, the base revenue requirement was approximately $170 million.

As initially filed, the application indicated a revenue deficiency of approximately $7.8 million.

A three-day settlement conference was conducted in this proceeding early this month at the Board's direction, and that was continued by the parties by way of a conference call.

Through the efforts of all of the parties, a settlement was reached on 26 of the 30 issues on the Board-approved issues list. Two of the remaining issues are partially settled and the final two are unsettled.

The settlement agreement was filed on Wednesday, October 24th, in keeping with the timeline in the Board's Procedural Order No. 3.

I will touch on the unsettled issues in a moment, but first I will mention a few highlights of the settlement agreement.

The settlement has reduced the service revenue requirement, increased slightly the revenue offsets, and reduced the base revenue requirement when compared with the amounts requested in the application.

The new service revenue requirement has been reduced from approximately 179 million to approximately 172 million, for a reduction of seven million. Revenue offsets have been increased from nine million to $9.8 million, and the resulting base revenue requirement has been reduced from $170 million to 162 million.

When revenue at current rates is taken into account, the 2013 test year revenue deficiency has been almost eliminated through the settlement. The settlement has reduced it by almost $7.8 million, so that from a revenue deficiency of $7,826,000, the 2013 test year revenue deficiency based on the settled issues will be $44,000.

For the purposes of settlement, the parties have accepted PowerStream's forecasted capital expenditures of approximately $114.3 million for the test year, and have accepted a reduction of approximately $6 million in OM&A, for a settled OM&A forecast of $80 million.

Finally, for the purposes of settlement, the parties have accepted the realignment of PowerStream's fiscal and rate years, an effective date of January 1st, 2013 for PowerStream's new rates and charges, and the harmonization of rates for PowerStream's north and south rate zones.

The parties are of the view that the settlement agreement will protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service, promote economic efficiency and cost-effectiveness in the distribution of electricity, and maintain the financial viability of PowerStream.

As a result of the settlement, the typical residential customer in PowerStream's south zone, which includes Markham, Vaughan, Richmond Hill and Aurora, will see a bill increase of 0.5 percent or 54 cents per month.

The typical residential customer in the Barrie zone will see a bill decrease of six percent, or $6.98 per month.

PowerStream and the other parties respectfully request the Board approve the settlement. PowerStream's witness panel would be pleased to answer any questions the Board may have about the settlement proposal.

Now, as I mentioned, there are two partially settled issues and two unsettled issues.

Those four issues are: Issue 2.1:

"Is the proposed rate base for the test year 2013 appropriate?"

Issue 4.2:

"Is the proposed level of the depreciation and amortization expense for 2013 appropriate?"

And I should mention that Issue 2.1 and Issue 4.2 are related.

Issue 6.1 is whether the proposed test year cost of capital parameters are appropriate.

And finally, Issue 8.2, which is the question of whether the treatment of property, plant and equipment due to the transition to the new accounting standards is appropriate.

PowerStream is presenting a single witness panel, and they will address those four issues in examination-in-chief. And in our letter to the Board last week, we suggested that all submissions be in writing and that the timing for those be November 7th for argument in-chief, November 21 for Board Staff and intervenor submissions, and November 28th for PowerStream's reply.

I am not aware of any objections to written submissions. I am aware that parties may have some comments on timing of those submissions.

Now, the revenue requirement shown in the settlement agreement reflects adjustments arising out of the settled issues.

For unsettled or partially settled issues, the agreement uses PowerStream's applied-for values.

The rate base and return on rate base may change as a result of the Board's disposition of the first three outstanding issues, and the Board's determination of the fourth issue may affect the balance for disposition in PowerStream's property, plant and equipment deferral account.

With those remarks, I will conclude my presentation of the settlement agreement, and when we do move into the hearing I will be presenting PowerStream's witness panel.

MR. QUESNELLE: Okay. Thank you, Mr. Sidlofsky.

MS. HARE: I do have a question about 2.1. My understanding of 2.1 is that there actually is agreement that whatever comes out of 4.2 will be applied to 2.1.

I mean, this isn't an issue, from how I read this, that is going to be the subject of evidence or cross-examination; is that correct?

MR. SIDLOFSKY: That's correct, Ms. Hare. What's driving the fact that Issue 2.1 is unsettled is the fact that there is -- there doesn't appear to be agreement on the treatment of depreciation.

MS. HARE: Right. So will that --

MR. SIDLOFSKY: Which is really -- I'm sorry -- which is really Issue 4.2.

MS. HARE: Right. So we will actually only have cross-examination on three issues?

MR. SIDLOFSKY: Essentially, yes.

MS. HARE: Okay. Now, I have a question that -- it is not questioning the settlement agreement, but it caught my interest, 3.1, where there was a change in the heating degree days from ten to eighteen.

But what caught my interest was, as a summer peaking utility, why do you look at heating degree days and not cooling degree days?

MR. SIDLOFSKY: Ms. Hare, I would love to answer that, but it may be better if one of the PowerStream representatives tries to assist the Board with that.

I have Mr. Macdonald here with me, Colin Macdonald. He will be one of the PowerStream witnesses.

I am not sure if you need him sworn for this answer?

MS. HARE: Maybe it makes no difference to the settlement agreement, but it piqued my interest, something that had this not been settled, we would have explored. Maybe it is something to think about for going forward.

But Mr. Macdonald, you look like you want to answer.

MR. MACDONALD: Well, if I may, certainly.

Well, the simple answer is, we do both. So we adjust for these cooling degree days and heating degree days. So it may have been worded so it sounds like we only use one, but we use the appropriate weather adjustment for each season. So we use both in fact.

MS. HARE: Thank you. 4.2; in the interrogatories, there were some questions about whether or not this shouldn't be the issue of the half-year rule, shouldn't be handled in a generic forum.

Is there agreement, then, that it should be addressed in this hearing?

MR. SIDLOFSKY: Madam Chair, I think it is something that needs to be addressed in this hearing, because it has a significant impact on PowerStream's rate base.

Ultimately, I suppose it is up to the Board in this proceeding to determine that it is more appropriately dealt with in a generic forum. But it is a matter for this proceeding. It has a significant impact on PowerStream's revenue requirement.

MR. SHEPHERD: I wonder if I could comment on that, Mr. Chairman, Ms. Hare.

I want to be careful to make sure that we don't give the wrong impression. I don't think all parties have agreed that there should be a new review of the issue of full-year versus half-year depreciation.

I think that an issue in this proceeding is whether the Board's policy is appropriate to apply in this case.

So I agree with Mr. Sidlofsky; the issue of what depreciation provisions should be used for PowerStream for 2013 is on the table here. But, I am not sure it is fair to say that we've all agreed that this is akin to a generic review of that issue.

The Board has a policy already, and certainly some of us don't think that we need to reargue that here.

MR. QUESNELLE: So to the extent that we have an unsettled issue, we have something to hear --

MR. SHEPHERD: That's true.

MR. QUESNELLE: -- in this proceeding.

MR. SHEPHERD: Yes.

MR. QUESNELLE: Thank you.

MS. HARE: Thank you. Those are my questions.

MR. QUESNELLE: Okay. Just one moment, please.

MS. SEBALJ: I just wanted to make sure we mark this, because I don't think it has been made an exhibit, it is K1.1.

EXHIBIT NO. K1.1: SETTLMENT AGREEMENT

DECISION

MR. QUESNELLE: Thank you, Ms. Sebalj; K1.1.

Based on the presentation and the responses to the questions, the Board is – the Panel has conferred, and we accept the partial settlement as presented and proposed, and thank the parties for their efforts in putting this together.

It is always helpful to the Board if great efforts are put to facilitate these settlements, and we like to see the fruits of those labours come forward. Thank you very much for that.

MR. SIDLOFSKY: Thank you, sir.

MR. QUESNELLE: With that, and I don't see any need to break at this time, Mr. Sidlofsky, if you could have your witness panel assembled, we will get right into the issues.

I don't know if there has been any discussion by parties as to the -- after your lead, Mr. Sidlofsky, of who will be going first, or what order will we will be attempting to do cross, Mr. Shepherd.

MR. SHEPHERD: Yes. I think I have drawn the short straw.

MR. QUESNELLE: Okay, thank you very much. Okay.

MR. SIDLOFSKY: Thank you, sir. I will ask the PowerStream witnesses to take their places in the witness area, thank you.

POWERSTREAM INC. – PANEL 1

Thomas Barrett; Sworn

Colin Macdonald; Sworn

Carolyn Young; Sworn

EXAMINATION-IN-CHIEF BY MR. SIDLOFSKY:

MR. QUESNELLE: Please be seated. Whenever you are ready, Mr. Sidlofsky.

MR. SIDLOFSKY: Thank you, sir.

Perhaps I could ask each of you to state your names for the record, starting with you, Mr. Macdonald.

MR. MACDONALD: Colin Macdonald.

MR. SIDLOFSKY: And Mr. Macdonald, I will get back to your qualifications in just a minute. But on your left we have Carolyn Young, correct? And on your right, Mr. Macdonald, is Tom Barrett.

MR. MACDONALD: That's correct.

MR. SIDLOFSKY: Now, this is probably an appropriate time to have a package of CVs entered as an exhibit. These are detailed CVs that were sent to the parties and the Board Secretary just over the course of the weekend. But I do have hard copies for the Board.

MR. QUESNELLE: Thank you. We have the CVs of the witnesses, Mr. Sidlofsky. Thank you.

MR. SIDLOFSKY: Thank you. I am going to begin with you, Mr. Macdonald. You are currently the vice president rates and regulatory affairs for PowerStream?

MR. MACDONALD: That's correct.

MR. SIDLOFSKY: And could you tell me what your responsibilities include?

MR. MACDONALD: Yes. I am responsible for rate applications, regulatory accounting, contributing to the regulatory strategy for the company, and also get involved in setting the corporate strategy for PowerStream.

MR. SIDLOFSKY: Sir, you have been with PowerStream from 2006, and I see that prior to that you were with Toronto Hydro, and one of its predecessors, Etobicoke Hydro.

MR. MACDONALD: Yes. My background is engineering and operations and I have moved through different jobs, and been in the finance rates area for about the last ten years.

MR. SIDLOFSKY: Sir, what are your responsibilities with respect to this application before the Board today?

MR. MACDONALD: I am responsible for the overall preparation of the application, and the various milestones that we go through towards getting a rate order eventually.

MR. SIDLOFSKY: Thank you, sir. Moving over to you, Ms. Young, you are the currently the vice president finance for PowerStream?

MS. YOUNG: Yes, that's correct.

MR. SIDLOFSKY: And I see you have been with PowerStream and Barrie Hydro since 2000, is that right?
MS. YOUNG: That's right.
MR. SIDLOFSKY: Okay. PowerStream itself since 2009?
MS. YOUNG: That's correct.
MR. SIDLOFSKY: And what are your areas of responsibility for the utility?
MS. YOUNG: Currently, my areas of responsibility are the accounting finance area, and that includes general accounting, corporate financial reporting, treasury and strategic decision support.
MR. SIDLOFSKY: You are a chartered accountant?
MS. YOUNG: Yes, that's correct.
MR. SIDLOFSKY: What are you responsible for with respect to this application?
MS. YOUNG: Specifically section 6, the cost of capital.
MR. SIDLOFSKY: And finally, Mr. Barrett; manager rate applications for PowerStream?
MR. BARRETT: Yes. My primary areas of responsibility are for the preparation of rate applications and regulatory accounting, which consists mainly of the deferral and variance accounts.
MR. SIDLOFSKY: I see you were with Aurora Hydro, which became part of PowerStream. And you were with Aurora since 2003, correct?
MR. BARRETT: That's correct.
MR. SIDLOFSKY: And with PowerStream for the past six

years?

MR. BARRETT: That's correct.

MR. SIDLOFSKY: Chartered accountant as well?

MR. BARRETT: Correct.

MR. SIDLOFSKY: And what are you responsible for in this application?

MR. BARRETT: In this application, I was responsible for a number of sections, but primarily to do with cost allocation and rate design, deferral and variance accounts.

MR. SIDLOFSKY: Was PowerStream's evidence prepared by you or under your supervision?

MR. BARRETT: Yes.

MR. SIDLOFSKY: Perhaps Mr. Macdonald?

MR. MACDONALD: Yes.

MR. SIDLOFSKY: Do you adopt it as your own evidence in this proceeding?

MR. MACDONALD: Yes, we do.

MR. SIDLOFSKY: And as we're all aware, there were numerous interrogatories and technical conference questions and undertakings given in this proceeding to date.

Do you adopt those responses and undertaking responses as your evidence?

MR. MACDONALD: Yes. There were a number of interrogatories and questions arose from the technical conference, and we were asked to do a number of different scenarios on different issues, which we did do.

We don't necessarily, you know, agree or endorse those various scenarios.

MR. SIDLOFSKY: And Mr. Macdonald, before I ask some questions about specific outstanding issues, I understand that you would like to give the Board a brief summary of those issues?

MR. MACDONALD: Yes, thank you.

So Mr. Sidlofsky just highlighted the issues. I would like to go into just a little bit of detail, and my colleagues, along with me, will go into a little bit more detail after that, but not great detail.

MS. HARE: I'm sorry, can I interrupt you on something, because I am looking at what you said?

You said you were asked to do a number of scenarios, and you don't necessarily agree with the scenarios but you certainly agree with what you agreed to in the settlement agreement?

MR. MACDONALD: Oh, yes, definitely.

MS. HARE: Thank you.

MR. MACDONALD: So first, as Mr. Sidlofsky mentioned, we were very pleased to reach a settlement in this case, and we definitely settled the big things, like capital, additions, OM&A.

And harmonization is a big milestone for PowerStream; it is a promise we made in -- going back to 2008, the merger with Barrie. So we're very pleased to harmonize rates between Barrie and PowerStream and have one set of rates. That is a big achievement for PowerStream.

I am also pleased to have the -- with a slight adjustment, the load forecast approved.

So we are left with four issues, two partially settled and two unsettled, and I would have to characterize these issues as technical. And as Mr. Shepherd alluded to, for one of the issues that actually applies to all their policy. I say there is a policy element to them, which is why the parties brought these to the Board.

So I will actually go, direct the Panel -- Ms. Hare, as you mentioned, actually Issue 4.2 is really where we start. And it has -- Issue 4.2 is on page 18 of the settlement proposal. And there is two paragraphs, a short one and a long one. The top of that section, the shorter paragraph addresses PowerStream's request for having a full year of depreciation in rates in the test year 2013.

The second issue, which is described in more detail, really gets down to the methodology that PowerStream used to calculate depreciation, and some discussion among the parties about how it is most appropriate to do that.

So that is two issues in depreciation, related but certainly different issues.

The next issue -- and we called this partially settled, because in cost of capital we did settle a number of issues -- the issue outstanding is the issue of the appropriate interest rate that should apply to the promissory notes that PowerStream has. We have three shareholders, Markham, Vaughan and Barrie, and they hold debt in PowerStream in different proportions. And this issue is brought to the Board due to the parties not being able to settle on the appropriate rate to apply to that debt in the test year.

The fourth issue, I think the most technical, is -- relates to the transition from Canadian GAAP to modified IFRS. So PowerStream did make that transition for this year, 2012. Necessarily, we had to do certain financials for 2011 to have a comparative year. And like all distributors applying for cost of service in 2013, we needed to make the application in modified IFRS.

So this unsettled issue relates to, I would say, the appropriate amounts and how to use this deferral account, this PP&E deferral account that the Board has established for all distributors. And this is a very big and important issue for PowerStream, as I believe we will explore as the morning goes on.

So, Mr. Sidlofsky, that is my overview of the four issues.

MR. SIDLOFSKY: Thank you, sir.

In my correspondence late last week, I may have mentioned that I would be beginning with Ms. Young, but I would like to do that.

And Ms. Young, my understanding is that -- as Mr. Macdonald discussed, is that the only matter that is at issue with respect to PowerStream's proposed long-term debt rate is the rate to be assigned to the three promissory notes held by the three shareholders of PowerStream; correct?

MS. YOUNG: Yes, that's correct.

MR. SIDLOFSKY: And what rate has PowerStream proposed for the shareholder debt?

MS. YOUNG: The rate for all three shareholders currently that we propose is 5.58 percent.

MR. SIDLOFSKY: And has that rate changed since the notes were issued?

MS. YOUNG: So there is the three promissory notes, two of them to the City of Vaughan and the City of Markham. You will notice some of the contracts say the Town of Markham is now a city, so I will refer to it as the City of Markham.

Those two promissory notes were issued in 2004 at a rate of 5.58 percent. This was when the OEB long-term rate was 6.9 percent. So that's always been in effect. The only change that was made is with the City of Barrie, and the City of Barrie, their shareholder note was originally issued in early 2000 at a rate of 6.5 percent, and it was lowered at a 5.58 percent rate in 2010. And there was an agreement during the merger that they would have the same rate for all shareholders, and so the City of Barrie at the time agreed to lower their rate to 5.58 percent so that all three shareholders would be having the same rate on their promissory notes.

MR. SIDLOFSKY: Ms. Young, what's your understanding as to why this is an issue in the hearing?

MS. YOUNG: So I believe the issue is really about callability of the shareholder debt. PowerStream has always looked at their shareholder debt as long-term debt, and as indicated on their financial statements, it is shown as long-term debt. We treat this debt as if it were not callable due to the conditions of callability specified in the promissory note.

So there is a requirement in the promissory note that they will sign a postponement agreement and postpone that debt, if the need arises, which they have all done, with the $200 million private debt issue that we just issued in August. So there is postponement agreements by all three shareholders.

MR. SIDLOFSKY: And could you briefly explain PowerStream's proposed approach to shareholder debt to the Board?

MS. YOUNG: Yes. The shareholder debt is an important part of the debt structure for PowerStream. Actually, currently our bank -- we bank with the TD, Toronto-Dominion Bank -- and they look at our debt as equity when they calculate ratios like debt-equity ratios. So it is an important component of our debt structure; there is definite advantages to PowerStream because of this.

And so if we look at the promissory notes, section 3.1 that we filed the OEB October the 12th, 2012, it does state the payments can be accelerated, but if you look at section 3.3, it clearly states --

MR. SIDLOFSKY: Ms. Young, could I just ask you to stop for a minute while the Board pulls that document up?

Thank you. That was filed October 12th.

MS. HARE: Well, while we're waiting for that to come up, can I ask a question that I actually meant to ask on the settlement agreement, page 24 of 32, which is what we're talking about.

It refers to, on the third line, items 4 to 10 in table 6.1. What about 11, which is not an affiliate, but the table refers to 4 to 10. Is 11 in that same category? Like should it actually read items 4 to 11, or 3 to 11? No, 4 to 11?

MR. MACDONALD: I am looking at the paragraph below the table.

MS. HARE: Hmm-hmm.

MR. MACDONALD: So it refers to items 1, 2, and 12.

MS. HARE: Right.

MR. MACDONALD: So --

MS. HARE: That's what we're talking about now.

MR. MACDONALD: Correct. Just to clarify, Ms. Hare, everything else was settled.

MS. HARE: Yes. So in the third line, where it says "will refinance in 2013, items 4 to 10", is that because number 11 was just entered into in August?

MS. YOUNG: The reason for the deferred interest portion, numbers 4 to 9, was due in 2013. That was the due date, which is next year. And same with the bank loan, the TD bank loan of the 50 million, was due next year also. So we have reflected --

MS. HARE: Okay, thank you.

MS. YOUNG: Yes.

MR. SIDLOFSKY: Ms. Young, I believe the Board has the document that you are referring to, so if you could continue, please?

MS. YOUNG: Yes. In section 3.1, it does identify with written notice the corporation has 90 days for acceleration of its debt.

But also in 3.3, at the bottom of the screen, any demand for accelerated payment is subject to the conditions of subordination. And we do have our debt currently subordinated and postponed, for the former EDFIN debt and now currently for the $200 million debenture, private debenture that we have just issued in August. So that has always been subordinated.

So the postponement agreement, we have issued those also and that is part of this same -- the same document that that you have up on your screen. In section 2, it outlines the restrictions on debt payments, and in that restriction on the debt payments - section 2, yes, that is the one – sorry, that is the promissory note.

So there is another document, the postponement agreements. I think if you -- let me just get the page. The postponement agreements start on page 11. So if you go to 13 of 55, it says

> “unless previously consented to in writing by the trustee or otherwise permitted under section 2, no payments in respect of any of the city notes may directly or indirectly be paid by the corporation to any of the cities, or received and retained by any of the cities in cash or other property, or be set off or any other manner prior

to the payment in full of all debentures."

So technically, we would have to pay out our debentures in order to pay off this promissory note, which as we understand contacting our bank, would be in the range of millions of dollars to actually cancel the $30 million promissory note -- or sorry. I shouldn't say promissory note. That would be the debenture, the private debenture, $200 million.

So we believe that it is effectively not callable.

MR. SIDLOFSKY: And, Ms. Young, what is the financial impact of this issue to PowerStream?

MS. YOUNG: So if the rate would change from 5.58 to 4.41, in the test year for 2013, it would be approximately $2 million.

MR. SIDLOFSKY: Sorry, that would lower the interest expense by the --

MS. YOUNG: Yes, lower the interest expense by $2 million.

MR. SIDLOFSKY: Thank you, Ms. Young.

Now, turning to you, Mr. Barrett. Perhaps we can begin with you.

Please -- could you please provide an overview of the approach PowerStream took to the calculation of depreciation in the application?

MR. BARRETT: Certainly. So we calculated depreciation for the -- what we call the historic or actual years 2010 and 2011. We have used the actual additions and we have used the actual in-service date.

So if it went in-service in January, it would be eleven months; if it went in in December, it would be one month of depreciation.

For the forecast years, the test year and bridge year, 2012 and 2013, we've used an estimate. For 2012 we've used an estimate -- average in-service date of six months on average. So that is sometimes referred to as the half-year rule. So we have used that for 2012.

We used an estimate for 2013, but that is tied to another aspect of this issue that Mr. Macdonald is going to deal with. So I will defer to him on that one.

MR. SIDLOFSKY: Mr. Barrett, what do you understand to be the outstanding issue related to your depreciation methodology?

MR. BARRETT: Essentially, we believe that we've followed the Board's guidance. Certainly the filing guidelines indicates that we should use an estimate for forecast year, or an estimate of the half-year rule or average of six months.

We also believe we followed the Board's guidelines in calculating actual depreciation on actual additions and their actual in-service dates.

Some parties don't think this is appropriate, or believe it is inconsistent.

MR. SIDLOFSKY: And, sir, what is the implication of this issue for PowerStream?

MR. BARRETT: Essentially, there was some evidence provided by interrogatories, recalculations that parties have proposed there would be adjustments to both rate base regarding 2010 and 2011, and there would be -- then they're proposing there would be an adjustment to depreciation, I believe, in 2012 and 2013, the depreciation estimates.

MR. SIDLOFSKY: And, sir, do you have concerns with alternative suggestions?

MR. BARRETT: We do. I have concerns. I believe that we’ve followed the Board's policy, particularly in the use of the six months' depreciation on the forecast years, which is in the guidelines and, we believe, is an appropriate method of estimating, and the best one that we have available for estimating the depreciation on the forecasted years.

We also take issue with the fact that I believe there's been -- there was a proposal that a different method be used in the Board-approved half year for the test year. Based on some of the history that was provided in the IRs for '10 and '11, we're not certain that is appropriate -- we obviously don't feel it is appropriate.

MR. SIDLOFSKY: Mr. Barrett, sorry. Could you tell me what that -- sorry. Can you tell me what that approach would be.

MR. BARRETT: I believe, because we use an actual in-service date for our depreciation, based on some of the evidence provided in responses to the IRs, it's being proposed that we somehow take -- that we take an approximation from the data for 2010 or 2011, or some combination thereof, and use that to estimate something other than an average of six months for 2013.

MR. SIDLOFSKY: And --

MR. BARRETT: Our position is that the six month or half year rule proposed by the Board is the more appropriate approach.

MR. SIDLOFSKY: Sorry, that was the -- you are speaking about 2012 there? Or 2012 and 2013?

MR. BARRETT: I think Mr. Macdonald is going to address 2013; I am responding to 2012.

MR. SIDLOFSKY: Okay. Thank you.

Now, Mr. Quesnelle, on Friday PowerStream had also provided an illustration that Mr. Macdonald will be referring to. I have provided copies to my friends and to Board Staff.

And perhaps we could have that marked as well.

MS. SEBALJ: Sure. First I am going to mark the CVs, if that is okay. I didn't get a chance to do that, so the CVs of the three witnesses will be K 1.2.

EXHIBIT NO. K1.2: WITNESS CVS

MS. SEBALJ: What I am about to pass to you, Panel, will be K .3.

EXHIBIT NO. K1.3: ILLUSTRATION PROVIDED BY POWERSTREAM

MR. QUESNELLE: Thank you. These were distributed to other parties on Friday, as well, Mr. Sidlofsky?

MR. SIDLOFSKY: Yes, they were, sir.

MR. QUESNELLE: Thank you.

MR. SIDLOFSKY: And so, Mr. Macdonald, Mr. Barrett said that PowerStream used an estimate of depreciation for the 2013 test year; is that correct?

MR. MACDONALD: Yes. We used an approximation method for 2013, but we used a full year of depreciation as opposed to a half-year depreciation.

MR. SIDLOFSKY: Can you explain to the Board why you did that?

MR. MACDONALD: Yes. I would refer the Board to the illustration that was just handed out, Exhibit K1.3.

And this is -- this is indeed a very simple illustration to make a point.

So in this illustration I have used an asset that is going into service in the test year, 2013; it has a value of $100. It has a 10-year depreciation life -- or 10 years –- a 10-year life, 10 years of depreciation. So that is $10 a year in depreciation.

So in the top part of this table where it says "half-year rule" the depreciation in rates using the half-year rule would be half of 10, or $5.

The accounting depreciation would be the same. As Mr. Barrett said, that's typical in Board-prescribed simplification of the half-year rule.

The problem arises in this simple example when, after rebasing -- so when we go into the IRM period – you can see in 2014 the depreciation in rates is $5. That is the amount that we got in 2013 rebasing.

But in real life, the accounting depreciation is $10, because we apply the accounting rule, 10 percent per year.

So you can see there is a funding shortfall in each of '14, '15 and '16. So that is the issue that we're bringing forward.

If you look at the bottom of the table, just to show what happens if you apply the full year -- perhaps it is obvious, but the depreciation in rates in the test year would be $10. The accounting depreciation would still be five for the half-year rule, but you can see during the 2014, '15 and '16 until the next rebasing -- this is according to third-generation IRM -- we're kept whole in terms of recovering in rates what it costs to have that asset.

So this is very, very simple, obviously, but you can layer on things here. If you had an addition in 2014, for example, which is real life, you would have additions in '14 and '15, the problem compounds because those -- those new additions don't have depreciation associated with them in rates.

So I didn't want to show that. I just wanted to keep it very simple, but as an illustration.

MR. QUESNELLE: Thank you.

MR. SIDLOFSKY: And, sir, finally on this issue, could you tell the Board what the implications are for PowerStream of this depreciation issue?

MR. MACDONALD: Yes. So the financial impact of this full-year depreciation for moving from a half to a full year, that is an additional $1.9 million of depreciation.

When you convert that to revenue requirement, it is

$2.5 million due to the tax adjustment, tax gross-up.

MR. SIDLOFSKY: Thank you, Mr. Macdonald.

Now, continuing with you, I would like to ask you to explain what the PP&E deferral account is, and what purpose it serves.

MR. MACDONALD: Certainly. Thank you.

The Board approved the PP&E deferral account for all distributors to help deal with an important aspect of the transition in accounting standards from Canadian GAAP to modified IFRS.

There are a number of changes in accounting or in -- a number of changes in financial information that result from this transition. To me, the two biggest by far are, one, IFRS is much more restrictive on the amounts that can be applied against capital projects; we're going to call it overheads or burdens. So the modified IFRS rules are much more restrictive, so the utilities can put much less of their costs against capital projects. So those have to be expensed otherwise.

So you will see that, typically with this transition to modified IFRS, OM&A costs go up, because those burden amounts can't be applied against capital. They go against OM&A.

There is an offsetting impact. There is a requirement also to have updated or better depreciation figures, or at least look at your depreciation.

So many utilities and the Board itself did a study of asset lives, so I think we were typical, and typical of what the Board did, as well. We found when we did the study that we -- we lengthened the lives for many assets. We determined from the studies that were done and from our own experience that assets were living -- lasting longer than we had used in the past, what we had seen in the past.

So the PP&E deferral account is used to sort of account for these differences, and make sure that utilities are kept whole during the process. That means that -- not just utilities but customers. So there is no -- you make the transition, there is no -- utilities don't gain, utilities don't lose. Same for customers; everyone sort of is equal.

MR. SIDLOFSKY: And how did PowerStream approach the establishment of its PP&E deferral account?

MR. MACDONALD: PowerStream followed the guidance in the -- there is a document, addendum to the Board –- to a report of the Board, implementing IFRS kin an incentive regulation mechanism environment. And that is the document where the Board approved the deferral account that I mentioned.

And PowerStream has captured the differences in PP&E between Canadian GAAP and IFRS arising in 2011 and '12, and we put those differences in that account.

MR. SIDLOFSKY: And when you applied that approach, what was the resulting balance, Mr. Macdonald?

MR. MACDONALD: We calculated a balance of $2.4 million, which is actually a refund to customers. So we had proposed to refund that over four years, or $600,000 per year.

MR. SIDLOFSKY: Sir, do you understand that approach to be compliant with the Board's guidance?

MR. MACDONALD: Yes. We strongly believe that we have fully complied with the Board's guidance in calculating the amounts for that PP&E deferral account.

MR. SIDLOFSKY: So could you explain the outstanding issue for the Board, Mr. Macdonald?

MR. MACDONALD: Yes, certainly.

PowerStream in a question was asked to calculate the balance on a different set of assumptions, and that increased the balance from $2.4 million to $9.6 million, a difference of $7.2 million. I believe that arose -- I stand corrected, but I believe it arose at the technical conference.

MR. SIDLOFSKY: Sir, was that -- did that change the balance from 2.4 million to $9.6 million to be refunded?

MR. MACDONALD: Yes.

MR. SIDLOFSKY: Okay. And, sir, what's your understanding of why this issue arises?

MR. MACDONALD: Well, this is where it gets increasingly complex, but the alternate basis or alternate suggestion ignores the fact that a portion of the differences in PP&E arising from this transition relate to construction work-in-progress.

It is typical in any given year that the -- the cycle of work doesn't match the 12 months of the calendar. So you quite often have work that you are not completing in the calendar year that goes into the next year. And next year, on it goes. Actually, in a given year you are going to have work from the previous year, obviously, that is coming into service, or coming into -- coming into service.

So under Canadian GAAP, this higher amount would have been -- gone to rate base in 2013. Unfortunately, under IFRS, the $7.2 million difference becomes an OM&A expense and never gets into rate base.

MR. SIDLOFSKY: That becomes an OM&A expense in what year?

MR. MACDONALD: The $7.2 million amount would become an OM&A expense in 2012. When I looked at this, I used the word "stranded" or "orphaned." The $7.2 million, which is part of construction work-in-progress or CWIP, it almost -- if we hadn't transitioned to Canadian GAAP, it would have just gone into the next year. It just would have been almost transparent to normal process.

But through this transition, and this sort of cut off at the end of this year for January 1, 2013, this amount of $7.2 million gets -- I think orphaned is a good word. We would have to write that off against our 2012 financial statements. So it is big. It is probably -- I think we calculated that it is about a quarter of our net income for the year would be the extent of the write-off. So that, that's the issue for PowerStream.

MR. QUESNELLE: The write-off would have to be done to accommodate -- or a reflection of the proposed methodology by others?

MR. MACDONALD: Yes. That's correct.

MR. QUESNELLE: All right. Thank you.

MR. MACDONALD: Exactly. We believe we accounted for this correctly. The alternate view has this -- again I will use the word orphaned, stuck and not being able to flow into the following year, and we would be faced with a write-off, which totally goes against the, you know, the Board's policy of, you know, utilities and customers not winning or losing on this transition, accounting transition.

MR. QUESNELLE: I understand the mechanics of it now, thanks.

MS. HARE: I actually don't understand.

So these are the amounts that you have recorded in the 2011 and 2012. But 2012 is not over, so it is an estimate for 2012, correct?

MR. MACDONALD: Yes.

MS. HARE: So why is this amount orphaned, if it is an estimate for 2012? Why wouldn't it be included?

MR. BARRETT: Perhaps I can clarify. The issue -- we have included all differences arising between the overhead that is capitalized in 2012 in our estimate.

In the alternate scenario, we were asked to base it on the fixed asset schedule, which effectively cuts off at December 31, 2012, and it ignores construction work-in-progress.

MS. HARE: I see.

MR. BARRETT: So the higher value of Canadian GAAP WIP that would have flown in under Canadian GAAP in 2013 into our rate base, our fixed assets, would -- that difference is never accounted for, the difference between the Canadian GAAP amount that is sitting in construction work-in-progress at the end of 2012, and the lower amount that is sitting there valued under IFRS, with a difference of about $7 million of overhead.

MS. HARE: And so that amount would be captured in the 2013 deferral account, which you wouldn't, then, be able to get any advantage of until you rebase next, in 2017? Is that what you are saying? So then it wouldn't be in rate base for four years?

MR. MACDONALD: No, our understanding is it is gone.

MS. HARE: It’s gone? Because the deferral account ends at the end of 2012?

MR. MACDONALD: No. It would be --

MR. BARRETT: Correct. I would say correct to that last one. Because we are rebasing in 2013, I believe that the deferral account --

MS. HARE: Ends?

MR. BARRETT: -- ends, yes.

MS. HARE: Okay, thank you.

MR. SIDLOFSKY: Now, just so I am clear, Mr. Macdonald. Is this an example of one of those calculations that you were asked to do, that you do not agree with?

MR. MACDONALD: Yes, it would be.

MR. SIDLOFSKY: Okay. In your view, is it in keeping with the Board's policy?

MR. MACDONALD: No. I won't quote the section from the addendum, but the Board report clearly identifies that during an accounting transition, in this case from CGAAP to modified IFRS, utilities shouldn't be at a windfall, nor be out of pocket.

So clearly it would not be in keeping with the Board's policy. And it is, you know, it's sort of nine times our materiality threshold. It is a big number.

MR. SIDLOFSKY: Thank you, Mr. Macdonald and thank you, panel.

Sir, those are my questions and the panel is now available for cross-examination.

MR. QUESNELLE: Thank you, Mr. Sidlofsky.

Mr. Shepherd, do you have an estimate of time that you will be requiring this morning?

MR. SHEPHERD: I would say my best guess is ninety minutes or so. But it is very fluid; it could be much less, or much more.

MR. QUESNELLE: Certainly. I would ask you to provide us with a natural break in your cross around eleven o'clock.

MR. SHEPHERD: Thank you, Mr. Chairman.

MR. QUESNELLE: Thank you.

CROSS-EXAMINATION BY MR. SHEPHERD:

MR. SHEPHERD: Let me start with a general question. You all know me, I think; Jay Shepherd from School Energy Coalition.

Your counsel said that you have a deficiency at the end of the day, before the issues that we're talking about, of $44,000. So it is basically zero, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: But it is true, isn't it, that your revenue requirement is about $5 million or so lower because of MIFRS? Your annual revenue requirement in the range of $5 million, right?

The mix of capitalized overheads and depreciation change is about a $5 million net reduction, right, or in that range.

MR. MACDONALD: No, I am not sure.

MR. SHEPHERD: Well, you know that for the two years, 2011 and 2012, it was 9.5 million. Right?

MR. MACDONALD: No.

MR. SHEPHERD: It was.

MR. MACDONALD: I am not sure where you are getting the numbers from. Can you help me?

MR. SHEPHERD: Yes, sure. The 9.5 million -- leaving aside CWIP, the 9.5 million is the PP&E account, right? So half of that is 4.7. So that is the difference each year, because both overheads and depreciation are in that number, right?

MR. MACDONALD: I am looking at Mr. Barrett, and we're both looking lost. I'm sorry. Is there something we could refer to, like a --

MR. BARRETT: We have booked the actual differences, and we believe the 2.4 million is the cumulative difference. So I am not sure where you are --

MR. SHEPHERD: I'm sorry, I’m not talking about -- I’m talking about revenue requirement now. I am just using that as a way of getting to it.

Look, there is an easier way of doing this. Can you undertake to provide us with the difference between revenue requirement on a MIFRS and CGAAP basis, for 2013?

MR. MACDONALD: Sure.

MR. SHEPHERD: Thank you.

MS. SEBALJ: So it is J1.1.

UNDERTAKING NO. J1.1: TO PROVIDE THE DIFFERENCE BETWEEN REVENUE REQUIREMENT ON A MIFRS AND CGAAP BASIS FOR 2013

MR. QUESNELLE: Thank you.

MR. SHEPHERD: And the other thing is, you have somewhere between five and seven million dollars of merger savings in the test year, right? I mean, it is built into the agreed settlement, I understand.

But nonetheless you still have between five and seven million dollars; that is in the evidence, right?

MR. MACDONALD: Yes, in our evidence, we did indicate that we had -- it is between. I think it is around $6 million in ongoing merger savings, that's correct.

MR. SHEPHERD: All right. So am I right in understanding that it is not fair to say that your -- that you don't have the rate increase in the normal sense, because you have a built-in deficiency because of those two items?

But for those items, you would have to ask for another

$10 million in rates, wouldn't you, roughly?

MR. MACDONALD: If we hadn't saved money through mergers or other things, our ask would be greater, yes.

MR. SHEPHERD: Yes, okay.

And $10 million would be about 6 percent increase, right, give or take? Am I in the ballpark?

MR. MACDONALD: Yes.

MR. SHEPHERD: Okay. So let's --

MR. MACDONALD: On a basis of 170, you're doing that about?

MR. SHEPHERD: Yes, 162 I think it is.

MR. MACDONALD: Yes.

MR. SIDLOFSKY: Sorry to interrupt, but that is also going to be subject to Mr. Macdonald's calculations of the difference between MIFRS and CGAAP.

MR. SHEPHERD: Of course, of course.

MR. SIDLOFSKY: All right.

MR. SHEPHERD: It is something.

MR. SIDLOFSKY: Understood.

MR. SHEPHERD: Okay. I just wanted to clear that up.

Now, let me deal with the last thing you dealt with first, because it is quite confusing, and so I want to just ask a couple of questions about that.

My understanding -- and tell me whether this is correct -- is Board policy says you take a snapshot of rate base on a CGAAP basis and a MIFRS basis, as of the beginning of the test year. And whatever that difference is, that difference is either refunded to or collected from ratepayers over the next four years.

That is what the policy actually says, right?

MR. BARRETT: No, I don't see that anywhere in the Board's report.

MR. SHEPHERD: Okay. Well, you are going to get to the Board report later, and you will see that it only says rate base and it doesn't say CWIP.

But I am just trying to get to the issue here, because I actually agree with you, Mr. Barrett, on this. I just want to make sure we're very clear on the issue.

If you just do it on rate base, you have a problem, because you have spending prior to the test year, spent in a CGAAP year, right?

MR. BARRETT: That's correct.

MR. SHEPHERD: And -- but it is going to be close to rate base under MIFRS, right?

MR. BARRETT: It will never -- because of the difference in accounting, it will never close to rate base under MIFRS. The difference will never close -- or the lower amount?

MR. SHEPHERD: Step by step.

MR. BARRETT: Okay.

MR. SHEPHERD: I am trying to make it simple.

Those capital additions will be close to rate base under MIFRS, right?

MR. BARRETT: Yes.

MR. SHEPHERD: Okay. The OM&A for the years where you spent the money will not include the capitalized overheads, because OM&A in those years is calculated based on CGAAP, right?

MR. BARRETT: For 2011, yes.

MR. SHEPHERD: Okay. And for -- and the capital additions, when you add them to rate base, will also not include those capitalized overheads, because that's being closed in a MIFRS year, right?

MR. BARRETT: Correct.

MR. SHEPHERD: So you have those capitalized overheads -- this is the only thing we're really concerned about here -- capitalized overheads that are not going to be in OM&A and they're not going to be in capital, because they straddle the period; is that true?

MR. BARRETT: I think your characterization is correct. They are -- they will be in OM&A under IFRS. I guess that is what is throwing me.

MR. SHEPHERD: Yeah, but see, the thing is they're not in your rates, right? Because your rates for 2011 and 2012 are based on CGAAP?

MR. BARRETT: That's correct.

MR. SHEPHERD: So you are not collecting that in OM&A. Those capitalized overheads are not being collected in OM&A, because your rates assume they're being capitalized, right?

MR. BARRETT: Yes. You are doing a better job of explaining this, yes.

[Laughter]

MR. SHEPHERD: I am trying to make sure that, if I am going to agree with you, I'm agreeing with the right thing.

But then when you close it normally, if you closed it to rate base it would be included in capital and everything would be fine, but because you are going from one accounting system to another, you don't get to include it when you close it to rate base either?

MR. BARRETT: That's absolutely correct.

MR. SHEPHERD: And that means that you lose that amount, the capitalized overheads for those two years, you lose it forever?

MR. BARRETT: That's correct.

MR. SHEPHERD: Okay. I have no further questions on that one. Let's go to the hard stuff.

Let's start with full-year depreciation. So as you said, you're seeking rates for 2013 that include full-year depreciation on capital additions in the year, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: And -- but from an accounting point of view, you're not planning to use full-year depreciation in your financial statements, right?

MR. MACDONALD: No. Not in the test year.

MR. SHEPHERD: Well, not in any year, right? New capital additions, you never will put full-year depreciation in, right?

MR. MACDONALD: No. They would have a full year after the -- in the year after rebasing.

MR. SHEPHERD: But not in the rebasing year?

MR. MACDONALD: Correct. We agree.

MR. SHEPHERD: Okay. So what you are asking the Board to approve is a different method for the test year, a different method for depreciation for accounting purposes and for regulatory purposes; is that right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: Okay. Are you proposing that, from now on, your rate base would be calculated using the full-year rule for all capital additions, each year?

MR. MACDONALD: No. This is a one-time request.

MR. SHEPHERD: Well, once you have a new accounting methodology approved by this Board, why wouldn't you continue to use it each year?

MR. MACDONALD: Well, the Board's issued a report on the new regulatory framework, and I need to come to terms with what that means. So I can't really -- I just can't say with certainty that we would make that request again.

MR. SHEPHERD: So the difference between full-year and half-year is $1.9 million. So what you are planning to do in the test year, what you are asking the Board to approve, is that you will collect 1.9 million more from ratepayers in rates than your actual depreciation expense, right?

MR. MACDONALD: Yes. For the test year.

MR. SHEPHERD: Okay. Well, we're talking about the test year. I mean, I understand there is an impact on subsequent years. We're going to get to that.

MR. MACDONALD: Yes.

MR. SHEPHERD: So doesn't that mean that at the end of 2013, your rate base will actually -- your real rate base will actually be $1.9 million higher than you are proposing in this application? Because you will have taken less depreciation than the Board has authorized?

MR. MACDONALD: Yes.

MR. SHEPHERD: And so how are you proposing to adjust for that? Have you proposed a variance account, like the PP&E account, to deal with that?

MR. MACDONALD: No.

MR. SHEPHERD: You are just going to -- so you are going to get it from ratepayers in the test year, but then it will still be in rate base and we'll pay for it again?

MR. MACDONALD: Well, we would -- according to the third-generation IRM, we would rebase again in 2017. That's the plan we're on. So that would be -- that would be accounted for in the next rebasing.

MR. SHEPHERD: How would it be accounted for? You're not proposing a variance account, so you are just going to have that extra 1.9 million in rate base that we have actually already paid for, right?

MR. MACDONALD: Yeah, but over the course of the asset, that will -- we won't end up ahead in any way.

MR. SHEPHERD: How is that?

MR. MACDONALD: Because the asset will be depreciated to the end of its life; the asset additions in 2013 would be depreciated to the end of their life.

MR. SHEPHERD: Help me understand that. Why did the Board have a PP&E deferral account when you changed from CGAAP to MIFRS, because there was a difference between the rate base that you actually had and the rate base that was assumed in rates? Why did the Board have that account, and you don't need one in this case?

MR. MACDONALD: Because we're just trying to address a funding issue beyond the test year.

MR. SHEPHERD: This is not about whether you have enough money to pay your capital additions, right?

MR. MACDONALD: It is.

MR. SHEPHERD: Well, but we have seen your financial statements. You have lots of money. You can borrow at 3.99 percent, as you just did, so you don't have a problem here with getting money, right? It is not a cash flow issue?

MR. MACDONALD: I wouldn't characterize it as cash flow, but I would call it -- we would call it a funding issue of having sufficient revenue to pay our costs including depreciation.

MR. SHEPHERD: All right. Your logic here is actually not about 2013. You agree that you shouldn't have full-year depreciation for 2013 by itself, right? Because that's not how much depreciation you are going to charge, right?

MR. MACDONALD: No, our issue is trying to address what happens after rebasing. You're correct.

MR. SHEPHERD: What happens in 2014 is several things, and tell me whether these are true.

The 2013 additions are now used for a full year, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: You have new additions in 2014 that are only used for part of the year; that's true?

MR. MACDONALD: That's correct.

MR. SHEPHERD: You have assets that went out of service in 2013 that will have a full-year impact on rate base in 2014, right?

MR. MACDONALD: Yes.

MR. SHEPHERD: And you will have new assets going out of service in 2014 that will have a partial-year impact?

MR. MACDONALD: Correct.

MR. SHEPHERD: Okay. And so those other three things, how have you addressed those in this proposal? You are addressing the full-year use of the 2013 additions in 2014; how are you addressing the other three things?

MR. MACDONALD: We haven't addressed them financially or with a request in revenue, but we have addressed them in our evidence as being –- actually, in a sense our proposal doesn't really address a lot of those issues financially. We will kind of be further behind because of some of the issues that you --

MR. SHEPHERD: Actually, some of these, you are further ahead, right?

MR. MACDONALD: Which one, for example?

MR. SHEPHERD: For example, assets going out of service?

MR. MACDONALD: Well, the problem is that when we bring new assets into service, they're at a higher value than the assets going out of service.

MR. SHEPHERD: Well, sorry, One thing at a time.

You have already adjusted for the new assets coming into service. Now I am talking about the ones that are going out of service.

You are treating that as zero, right?

MR. MACDONALD: Yes.

MR. SHEPHERD: Okay. Then in addition to assets going out of service, you also have assets each year that reach the end of their depreciation, but they're not out of service, right? You finished depreciating them?

MR. MACDONALD: There would be. There would be.

MR. SHEPHERD: In fact, we know it is a fairly big number, right? It is like 12, $14 million a year?

MR. MACDONALD: I don't know the number, but I know there is always going to be assets that are going out of service.

MR. SHEPHERD: I wonder if you could turn up School Energy Coalition No. 17.

And my apologies, Mr. Chairman, I have not been able to put together a compendium today. I am not referring to a lot of things, so hopefully it won't be a problem.

MR. QUESNELLE: Thank you.

MR. SHEPHERD: So if you would take a look at SEC No. 17 -- it is in the IR responses. You want to look at your IR responses. It is 4.1. Is this the IRs?

You know what? Why don't I find you the page number? It is page 682. So do you see that?

We asked you what the original cost is of the assets going out of service each year. Do you see that? You have totals at the bottom.

MR. MACDONALD: I do remember this IR, yes.

MR. SHEPHERD: In fact -- so for this year, for example, it's $12.2 million?

MR. MACDONALD: Yes.

MR. SHEPHERD: And next year it is $14.2 million?

MR. MACDONALD: Yes.

MR. SHEPHERD: Sorry. Is that -- let me just.... sorry, for next year it is 12.2 and for 2014, it is 14.2. So what that means is that when they go out of service in that year, then your depreciation is lower, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: Because you don't have depreciation on those anymore?

MR. MACDONALD: That's correct.

MR. SHEPHERD: So that is, what? A million dollars? In each case, you're talking about a million dollar reduction in depreciation, or so?

MR. MACDONALD: That's correct.

MR. BARRETT: That's correct, but in 2014, likely there is going to be additions in so much of the test year. These are -- you are right. There is some amount of depreciation being provided during the IRM period from fully depreciated assets. But I think if you look at the schedule, it shows it is nowhere, it’s not going to be anywhere near at the level of additions.

MR. SHEPHERD: You are not adjusting for both factors, are you? You are only adjusting for the half-year rule for the additions in 2013. You are not saying, oh and by the way, we have to offset that against the stuff that we stopped depreciating in 2013, so that we don't have that depreciation any more.

MR. BARRETT: The things we stopped depreciating in 2013 have already been considered in the test year. They have already come out. I mean --

MR. SHEPHERD: But you are worried about 2014. Keep this, keep focussed here on 2014.

MR. BARRETT: Hmm-hmm.

MR. SHEPHERD: You're saying 2013, you only need half-year rule. It is 2014 that you need full-year rule.

MR. BARRETT: Correct.

MR. SHEPHERD: And -- but in 2014, you also have less depreciation because of these assets going out of service, right?

MR. BARRETT: And we also have brand new additions which – indeed, indeed, of a far greater magnitude than these numbers, so I not quite sure what --

MR. SHEPHERD: Well, I guess I am concerned that you might be cherry-picking. You’ve got this $1.9 million extra that you want, but you're saying, but let's not -- let's ignore that other one million there. And I’ve got more, so --

MR. BARRETT: If I understand you correctly, you're suggesting that the depreciation that would be provided by these fully depreciated assets that we're looking at here, would provide enough to cover the shortfall from 2013. But my understanding under IRM is these are supposed to provide depreciation for the new additions, which would be far in excess of this.

MR. SHEPHERD: Well, but we're not finished yet. There is other impacts too, right.

So for example, on the 2013 additions, you are only allowed to take half of the normal capital cost allowance in calculating your taxes, right?

MR. BARRETT: Correct.

MR. SHEPHERD: And if you took full CCA, your taxes would be lower. So would your rates, right?

MR. BARRETT: Presumably, yes.

MR. SHEPHERD: So can you tell the Board the dollar impact, if you were to calculate your 2013 taxes on the basis of full-year CCA?

MR. BARRETT: It is not an option. I could calculate an amount, but it is not an option. I am only allowed to take a half year on additions in 2013 for tax purposes.

MR. SHEPHERD: Yes. And you are only allowed to take depreciation for accounting purposes at half year as well.

MR. BARRETT: Yes, absolutely.

MR. SHEPHERD: I am not making stuff up here.

MR. BARRETT: No.

MR. SHEPHERD: But for 2014, you will get full year, right --

MR. BARRETT: Yes.

MR. SHEPHERD: -- on those additions. So why isn't it the same?

MR. BARRETT: You are correct. It would be -- the diminished value would be subject to -- there would be a full year's in 2014. There’s many moving parts to this, yes, I agree.

MR. SHEPHERD: And in fact, the difference in CCA is about $2.6 million. Would you accept that, subject to check?

MR. BARRETT: Subject to check.

MR. SHEPHERD: And that would reduce rates by about $900,000? If you had $2.6 million increase in CCA, then all other things being equal, your rates go down by about $900,000, right?

MR. BARRETT: Subject to check, once again, sure.

MR. SHEPHERD: So that is not insignificant, right?

MR. BARRETT: No. I'm agreeing with you that there are many moving parts to this.

MR. SHEPHERD: It is true, isn't it, that some of the capital spending is for new customer attachments in your service area, right? The additions in 2013 include customer attachments, right?

MR. BARRETT: Yes.

MR. SHEPHERD: What is your growth rate? Two percent? 1.8?

MR. MACDONALD: A little below two.

MR. SHEPHERD: Okay. So capital additions are pretty significant. Those customer attachment additions are pretty significant, right?

MR. MACDONALD: That's still part of what we do, yes, absolutely we connect customers.

MR. SHEPHERD: But when you add customers during 2013, you are not including the full year's revenue in the calculation of your rates for those customers, right, because they're not customers for the full year?

MR. MACDONALD: No, there’s a -- when we do our load forecast, there is a similar assumption to the tax -- like the customers don't all arrive January 1, nor December 31.

So they're assumed to be equally spread across the year.

MR. SHEPHERD: The half year rule, in other words?

MR. MACDONALD: We don't call it that. But in effect that is what it is.

MR. SHEPHERD: Okay. But in 2014, you will have the full-year revenue of those --

MR. MACDONALD: Those customers will be assumed to have been in place at the beginning of that year, that's correct.

MR. SHEPHERD: And how much is that? What is the difference between a half year and full year for that revenue?

MR. MACDONALD: I don't know the amount of revenue.

MR. SHEPHERD: Can you undertake to provide that?

MR. MACDONALD: Sure.

MR. SHEPHERD: Okay.

MS. SEBALJ: That is J1.2.

UNDERTAKING NO. J1.2: TO PROVIDE THE DIFFERENCE BETWEEN THE HALF-YEAR AND THE FULL-YEAR REVENUE FOR CUSTOMERS ASSUMED TO HAVE BEEN IN PLACE AT THE BEGINNING OF 2014

MR. SHEPHERD: Now, the other part of this, I think, is that some of your spending in 2013 is for capital to serve subdivisions and new customers that won't actually be attached until 2014, right?

MR. MACDONALD: That invariably happens, yes.

MR. SHEPHERD: In fact, that would be a fairly substantial amount, right? Because for example, a new subdivision, a lot of the spending happens the year before the homes are actually sold and occupied, right?

MR. MACDONALD: That could be true, and it could be true over actually a number of years, yes.

MR. SHEPHERD: But that impact, that increase in revenue on 2014, you have ignored that as well, right?

MR. MACDONALD: Well, that's to us, I think -- isn't that a revenue coming later?

MR. SHEPHERD: Well, no. It is coming in the year you are worried about. You are worried about 2014. You're saying, we're going to get ripped off on depreciation in 2014, because 2013 only includes a half year rule.

So I am saying, well, what else are you going to get in 2014? You are certainly going to get the new customer attachments in 2013; they're going to give you more revenue.

You're going to have spending in 2013 that has 2014 revenues, additional revenues from new attachments.

You are going to have capital cost allowance on a full-year basis, and you are going to have things going out of service.

You haven't included any of those, right?

MR. MACDONALD: No.

MR. QUESNELLE: Mr. Shepherd, could I ask, just for clarification, how you differentiate between the comments you are making on the growth rate being two percent and the growth associated with the construction of new subdivisions?

MR. SHEPHERD: Yes. I am distinguishing -- these are actually questions from Mr. Aiken, who was unfortunately unable to be here today. So it is actually my fault if it is not understandable. If he asked them, everybody would be able to understand them.

There are some attachments that happened in 2013. They produce revenue, but only half of it is included in 2013 and the rest in 2014.

There are also some spending in 2013 that doesn't create any attachments, but is going to in 2014.

So that's additional revenue in 2014 as well, from a separate source.

MR. QUESNELLE: I will take the blame for that, Mr. Shepherd, because you said it exactly the same way a minute ago, and now I get it. So thank you.

[Laughter]

MR. SHEPHERD: All right. So I guess what I'm trying to understand is why you didn't look at all of the impacts and say, what are all of these various impacts and what's the result? Why just pick one?

MR. MACDONALD: Because we were trying to find a simple way to solve a funding problem during the IR period. Maybe even creative.

MR. SHEPHERD: Now, you talk about this as a funding problem during the IR period.

Mr. Chairman, I wonder if this is a good time to take a break.

MR. QUESNELLE: Certainly. We will recess until 11:15 and return then. Thank you very much.

--- Recess taken at 11:00 a.m.

--- On resuming at 11:21 a.m.

MR. QUESNELLE: Thank you. Please be seated.

Feel free to continue, Mr. Shepherd, whenever you are ready.

MR. SHEPHERD: Thank you, Mr. Chairman.

So when we left off, you had just said that what you were trying to do with this full-year depreciation is solve a funding problem during the IRM.

It is true, isn't it, that a number of LDCs argued strenuously on this point in the Renewed Regulatory Framework for Electricity? Right?

MR. MACDONALD: Very much so, yes.

MR. SHEPHERD: And did the Board include a change to that in the report on regulatory framework for electricity?

MR. MACDONALD: Not that I can see.

MR. SHEPHERD: So I guess I'm trying to understand -- why are you arguing for it here when you've just argued and the Board hasn't implemented it in a broader context?

MR. MACDONALD: Well, we brought this forward in May. This predates the Board's report on renewed regulatory framework.

MR. SHEPHERD: All right. But you're not withdrawing it?

MR. MACDONALD: No.

MR. SHEPHERD: The Board did, in the renewed regulatory framework report, offer a new method, which I think is called custom IR, which is basically like a multi-year cost of service, right?

MR. MACDONALD: Yes.

MR. SHEPHERD: You have that available to you starting in 2014, don't you?

MR. MACDONALD: I believe, yes, May 2014.

MR. SHEPHERD: But if you took that approach, if you took the custom IR approach, as it is called in the report, you would have to include all of those other impacts that we were talking about, right? You couldn't just include full-year depreciation; you would have to factor in all of the other impacts that we talked about, CCA, things going out of service, et cetera, right?

MR. MACDONALD: I -- I don't know. I don't know enough about the report. Actually, I don't think there is enough details, at least for me, to determine that.

MR. SHEPHERD: All right. Let me turn to the second depreciation question.

So in order to keep this as simple as possible, let's pretend you didn't ask for full-year depreciation for 2013. Let's pretend that you had filed on a half-year basis. Okay?

MR. MACDONALD: Agree.

MR. SHEPHERD: Just so that we can simplify this monthly in-service question.

MR. MACDONALD: Agree.

MR. SHEPHERD: In 2009, you had a cost of service -- your rates were set on a cost of service basis, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: And those rates were approved on the assumption that you were using the half-year rule for depreciation?

MR. MACDONALD: That's correct.

MR. SHEPHERD: But in 2010 and 2011, you didn't use the half-year rule. You used monthly in-service, which is a more accurate accounting method, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: And you use it because it is more accurate?

MR. MACDONALD: Yes.

MR. SHEPHERD: Did you get an accounting order allowing you to change your depreciation methodology?

MR. MACDONALD: No.

MR. SHEPHERD: Will you accept -- I could take you to the evidence reference, but I think you probably know these numbers. In 2010, your depreciation on a half-year basis would have been 750,000 more than on a monthly in-service basis; is that right?

MR. MACDONALD: Are these, Mr. Shepherd, the numbers that came up through IRs?

MR. SHEPHERD: Yes. These are the numbers from Energy Probe 32. I am just trying to avoid having to go to the --

MR. MACDONALD: Well, effectively it is in the settlement proposal, agreement that we looked at today, right?

MR. SHEPHERD: And in addition, in 2011, when you were actually on MIFRS, right? Because it is your prior year?

MR. MACDONALD: Yes.

MR. SHEPHERD: So in 2011, on a MIFRS basis, the half-year basis would be 513 more than you actually claimed, right?

MR. MACDONALD: That was the response to that IR. That --

MR. SHEPHERD: Are these numbers not correct?

MR. MACDONALD: Those are correct numbers, but I think it is important to indicate that those are -- that's for those years. I mean, there could be different in any other given year. They could be reversed.

MR. SHEPHERD: Well, we're going to get to that in a second, but I guess I am -- I want to make sure I understand that your approved method was half-year rule, right?

MR. MACDONALD: I am not -- I disagree with that. I'm not aware that for us to go from half-year assumption in 2009 to monthly in-service additions requires an accounting order. I don't think it requires an accounting order from the Board.

MR. SHEPHERD: So you can just change your depreciation method any time you like and the Board doesn't care?

MR. MACDONALD: I didn't say that. I said we can go to a more accurate method without a Board's accounting order. That is my understanding.

MR. SHEPHERD: And who gets to decide that? You do? The Board doesn't care?

MR. MACDONALD: Yes. I don't know -- my understanding is that a Board accounting order is not required to make that change.

MR. SHEPHERD: All right. What is your basis for that?

MR. MACDONALD: We made a decision as a company to move to a more accurate accounting method or depreciation.

MR. SHEPHERD: But your rates were set on a different basis?

MR. MACDONALD: Yes.

MR. SHEPHERD: So can you do with that anything? Can you go to a more accurate method for anything, and not worry about what your rates were set on?

MR. MACDONALD: I don't think you could do it for anything.

MR. SHEPHERD: Well, what is special about depreciation?

MR. MACDONALD: I'm not sure there is anything special about depreciation. That is a decision we made in 2010, to adopt a more accurate way to book assets and calculate depreciation.

MR. SHEPHERD: And the total difference between the two years, 2010 and 2011, is a million 263, right?

MR. MACDONALD: That is the difference between -- if we had used the half-year simplification.

MR. SHEPHERD: And so as a result, your rate base as of January 1st, 2012 was a million 263 higher than it would have been had you used half-year rule; correct?

MR. MACDONALD: On the hypothetical, yes, based on the IR response, yes.

MR. SHEPHERD: Well, either it is accurate or it is not?

MR. MACDONALD: Well, we will stand by our response to the IR.

MR. SHEPHERD: Okay. So then in 2012 -- well, let me back up a second.

Those two years, the monthly in-service is a lower depreciation amount than the half-year rule. This is actually a natural thing, right? Because your construction cycle makes it more likely that you are going to close things to rate base in the last half of the year than the first half of the year, right?

MR. MACDONALD: I am not sure I could agree with that. It could depend on different mixes of projects in any given year.

MR. SHEPHERD: Okay. No, that's great. Because I think this is actually true, and so I am going to ask you to undertake to give us the calculations for as many years back as you can do, the difference between monthly in-service and half-year rule. Give us as many years as you have, and see if we can find one where that is not true.

MR. MACDONALD: So a reasonable number of years? Okay, certainly.

MR. SHEPHERD: Thank you.

MS. SEBALJ: J1.3.

UNDERTAKING NO. J1.3: TO PROVIDE CALCULATIONS FOR AS MANY YEARS AS POSSIBLE FOR THE DIFFERENCE BETWEEN MONTHLY IN-SERVICE AND HALF-YEAR RULE.

MR. SIDLOFSKY: Sorry, could we get some scope on the number of years?

MR. SHEPHERD: I am leaving it to Mr. Macdonald. He's going to want to go back until he finds a year that the opposite is true, and I think it might be a lot of years.

MR. MACDONALD: The thing that went through my mind is just having various mergers, different sets of data, but I take your point and we will do our best on that.

MR. SHEPHERD: So now in 2012, for the purposes of this application you forecast depreciation for this year using the half-year rule, right?

MR. MACDONALD: That's correct.

MR. SHEPHERD: But you are not going to use the half-year rule for accounting purposes, right?

MR. MACDONALD: For --

MR. SHEPHERD: '12.

MR. MACDONALD: '12? No, when the year is done, we would have used monthly -- well, let me correct that.

We will be using monthly in-service additions.

MR. SHEPHERD: So, again, you will be using a different method than the method on which this application is based?

MR. MACDONALD: Yes, but when we filed, the only way we had to do depreciation for 2012 was the half-year rule.

MR. SHEPHERD: If the past pattern plays out, you will have a further $500,000 difference between your depreciation on the half-year rule and the monthly in-service, right?

MR. MACDONALD: If 2010, 2011 are typical years in the same relationship to in-service additions versus half-year rule, then yes, I would agree with that.

MR. SHEPHERD: And that means that your rate base will be overstated at the start of the test year by perhaps a million eight, too? Something like that?

MR. MACDONALD: If that relationship is true, yes.

MR. SHEPHERD: So at this point, it is now the end of October. You must have a pretty good idea of what your monthly in-service dates will be for 2012, right?

MS. YOUNG: Just a few points on that. We do budget using the half-year rule. As Mr. Colin said at the time, that is the best information we have.

Usually, what happens in the accounting world is that it takes significant amount of time to go through the work-in-process account -- that is where all of the jobs are -- and allocate that to -- to the fixed assets.

So there is sometimes a retroactive-type of adjustment made for the year for those additions.

So at this point right now, I can't say with any certainty on when those additions -- we make assumptions through the year, and it is really at year-end where we get a really good number and an estimate on -- when we close those jobs, for the capital.

MR. SHEPHERD: Ms. Young -- Ms. Young?

MS. YOUNG: Yes.

MR. SHEPHERD: Mr. Glicksman gets a report every month on what has been closed to capital in that month, doesn't he? Isn't that in fact true; every month? You know from operations. You know from operations exactly what you have completed and put into rate base every single month? Isn't that true?

MS. YOUNG: I do not believe so. I wish we were that effective, and we're working towards that. But, no, right now, there is definitely analysis of a work in process is to make sure, and talk to the engineers, has this been closed.

Lots of times jobs tends to stay open quite a bit longer than they should, because we're waiting for an invoice.

So there is definitely a delay. We're trying to get better at that. But at this point in time, everything goes into this work in process account and then gets allocated to capital. So it is a quite involved process.

MR. SHEPHERD: I understand the accounting is quite involved.

But your operations people actually know what projects they’ve finished, don't they? They have a list.

MS. YOUNG: They try to keep on -- up on that list. The communications to the accounting department is sometimes slower. And, again, that is what we're working towards.

I think, you know -- I started in the finance area in January. But if Mr. Macdonald -- if you would like to confirm that for me? He used to be, for many years, involved in the accounting department.

MR. MACDONALD: I agree. We do a decent job of -- we're getting better at tracking capital additions. But the issue of monthly in-service date for depreciation, we have some -- for the current year, we do have some work to do.

MR. SHEPHERD: And I understand that. But I guess what I also understand is that your executive has to keep on top of whether capital projects are being completed on time and on budget.

That is something they have to do; and they do it, right?

MR. MACDONALD: Yes, we do have a monthly report, as I mentioned, of capital additions by category.

MR. SHEPHERD: Okay.

MR. MACDONALD: But not a -- Mr. Glicksman, you know we were close together. I am not aware we ever looked at a depreciation schedule --

MR. SHEPHERD: I didn't ask about depreciation. I just asked about capital --

MR. BARRETT: If I could clarify, I believe it is capital spending; not additions to fixed assets, but actual capital spending on projects. I don't believe it --

MR. MACDONALD: It is project management type view. It is how projects are progressing.

MR. SHEPHERD: If this is the report I think it is, it also has what closed -- what projects were completed in the month and whether they were completed on time, right? Every single month, you get that.

MS. YOUNG: There is a spending report, and like Mr. Barrett mentioned -- there is a spending report. Communications to the accounting and the actual booking of the fixed asset, which ends up, I believe, in the rate base, is a little slower in that process.

There is a much better handle in the capital projects as done in engineering area. There is more diligence, especially for the large projects, on the spending. The actual booking it to fixed assets is the slower part, which --

MR. SHEPHERD: And it is also true that now, at this point, you also know what projects you are expecting to complete next month and the month after, right? Because, again you have to be on top of those in order to manage your business.

You have a lot of people doing this, and you've got to know whether you are going to finish them on time, right?

MR. MACDONALD: Well, you're painting a picture that is making us sound a little bit better than we are, I think. It is not -- we haven't perfected it to that level.

MR. SHEPHERD: All right. So here's what I'm trying to get at. I would like you to give us, if you could, a month-by-month capital closed to rate base -- or capital additions, projects finished, by dollars, month to month, for as much of this year as you can give me.

MR. MACDONALD: We can do that, certainly.

MR. SHEPHERD: Okay.

MS. SEBALJ: That is J1.4.

UNDERTAKING NO. J1.4: TO PROVIDE CAPITAL ADDITIONS, PROJECTS FINISHED, BY DOLLARS, MONTH TO MONTH, FOR 2012

MR. SHEPHERD: I would like to say that is the end of this thing. But it isn't, because in 2013 -- again, we're assuming that the Board orders you to use the half-year rule, or accepts that the half-year rule is the appropriate way to go.

But you are still in fact, for 2013, going to use monthly in-service, right?

MR. MACDONALD: Yes. So just to be clear, for any year that is completed, when the year is completed we will have used monthly in-service additions.

So sometime in 2014, you are correct, we will have a view of 2013 depreciation that we based on monthly in-service additions.

For forecasting, like when we're doing a rate application looking forward, we use the simplification of the half-year rule.

But for completed years we would have used monthly in-service additions.

MR. SHEPHERD: And so if you were actually going to recover in rates the depreciation you actually expect to charge in 2013, you would have to forecast on a monthly in-service basis, right?

That would be the most accurate way to do it, because that is how you are going to account for it.

MR. MACDONALD: If you could -- I don't know, because -- I don't know how -- so this application is done in 2011 and 2012, filed in May. I don't know how well you could forecast for 2013 monthly in-service additions.

I am not trying to be difficult.

MR. SHEPHERD: No, I understand.

MR. MACDONALD: I am trying to picture what it would look like. We would have to sit down and figure out which, of all of these projects of when roads are widened, we move poles and all of these things, and it is very hard to speculate.

There might be a pattern, as you’ve mentioned, from the past. But it would be hard to speculate exactly when they go in-service. There is so many moving parts.

MR. SHEPHERD: You do have to plan for it, though.

Operationally, you’ve got a whole lot of people out there doing this stuff. And so you do have to plan on a month-by-month basis, don't you?

MR. MACDONALD: Well, I think we're good at doing the design and planning, that -- you know, the pure design and planning for those projects.

In terms of delivery during the year, in terms of having a process for really having optimal use of all of the crews, and all of the projects timed, I am not sure how advanced we are in that yet.

MR. SHEPHERD: Have you ever looked at whether there is a pattern to your spending, your completion of projects during the year? Have you ever looked at whether there is a pattern?

MR. MACDONALD: No.

MR. SHEPHERD: Okay.

MR. MACDONALD: Only -- only having in hindsight, you know, the monthly in-service additions.

MR. SHEPHERD: Well, no, I am just a little surprised because you went -- in 2010 you went to monthly in-service dates, and I would have thought -- I know some of the people in your utility, and I would have thought that somebody would have said, well, what difference is this going to make. Tell us what the difference is. Go back and look at the past, and give us an analysis.

Nobody did that?

MS. YOUNG: If I can just mention -- I believe when we merged the practices is when this came about.

So as Barrie Hydro, the former Barrie Hydro, I believe they used in-service dates. And when we merged, PowerStream used the half-year rule for accounting.

And so this is when this transpired. We looked at the half year; we looked at the in-service dates. And I believe, under modified IFRS, we actually have to go to in-service dates. I don't think they’d allow the half year.

So when we went to this method, it was a matter of looking at Barrie and PowerStream, and figuring out which method would be the best to use. That is why a decision was made to change to in-service dates.

MR. SHEPHERD: Sorry. Let me just make sure I understand.

Are you saying that IFRS requires monthly in-service dates?

Because, I mean, Mr. Barrett and I sat on the committee and that never came up.

MS. YOUNG: We were talking to an individual in our office, who is very versed in IFRS, and it is of her opinion that under IFRS, I don't think you could just use a half year.

Now that's different for forecasting, obviously. IFRS doesn't deal with forecasting. What they're dealing with is your actual financial statements.

MR. BARRETT: I spoke with our manager who was in charge of our IFRS project, and she looked up the IAS or whatever and confirmed to me that, yes, IFRS is that precise. Just like they insist we be precise on the useful lives, they also insist we be precise in depreciating, that we depreciate it based on when it goes in service, rather than estimating.

MR. SHEPHERD: That is interesting, okay.

MR. BARRETT: Just to be clear, though -- just to be clear, we didn't -- the decision to go from 2009 to 2010 and change our methodology wasn't based on IFRS.

It was based on the harmonization that Ms. Young referred to. But retrospectively, IFRS, you know, would have required it, or requires it.

MR. SHEPHERD: I understand that, Mr. Macdonald.

But I guess one of the possible options for the Board this year is to say, you're authorized to use monthly in-service dates going forward, and recalculate your depreciation to be appropriate for that purpose.

And presumably, if it is required for IFRS purposes, that might influence the Board's decision in this. That is what why I am trying to run down whether it is a requirement or not.

MR. MACDONALD: My understanding is that it is a requirement, yes.

MR. SHEPHERD: Wonderful. Thank you.

The last area is the interest rates on the shareholders' loans, and --

MR. QUESNELLE: Mr. Shepherd, just before you go there, I was trying to catch you as you were changing gears there.

But just on this last item, I am understanding better what the impetus was of going to the monthly in-service dates.

But when you were -- I am sure this happened on a myriad of approaches to things, looking at Barrie versus the PowerStream and the many ways that PowerStream looked at it in its original kind of set-up and looking at the various utilities.

Was that the -- what was the judgment? Why was it judged that the monthly was preferred, as a -- other than it just being more accurate?

MR. MACDONALD: Well, you are correct, Mr. Quesnelle, that in a merger there's dozens and dozens of processes that you can look at and take the best, or something else. So this was one of them.

I would have to say the decision was made for accuracy. It was made for accuracy.

MR. QUESNELLE: Accuracy, and what I am catching -- and I think Mr. Shepherd was kind of alluding to it earlier -- the accuracy, it seems, is in there after the fact, but it is not a leading indicator of anything.

MR. MACDONALD: Correct. That is why we have adopted this methodology for this application. So we have two years, 2010 and 2011, of actual, and presumably more accurate data. But necessarily for 2012 and '13, we used a forecast half-year rule because we don't have a capability to do forecasting on a monthly basis.

I am not sure when we would have that or if it is appropriate. So it is a mix-and-match.

MR. QUESNELLE: Inherent in that is the symmetry of treatment of your --

MR. MACDONALD: Yes. I think it is necessary. And I think from understanding the Board's okay with that, from what we have understood in the past.

MR. QUESNELLE: Well, it is an issue here.

[Laughter]

MR. MACDONALD: Well, in the past. During this application, we didn't think we were out of step with others.

MR. QUESNELLE: I am not making the point of whether or not you've used it in the past. It's its application here in this application which is at issue, obviously.

MR. MACDONALD: Yes.

MR. BARRETT: Perhaps I could make a comment.

I think your basing on in-service date is just -- the question is we're using six months on average as our average in-service date. It is just -- I think it is a question of the estimating tool.

MR. QUESNELLE: Understood. Okay. That puts it in perspective. Thank you.

MR. SHEPHERD: Just to -- I was going to go to the next thing, but now I am interested.

You have no reason to believe that six months is the correct estimating tool, right?

MS. YOUNG: If I may comment that we still for budgeting purposes use six months, we still use that internally as our guideline for capital additions.

So that is still what we use.

MR. SHEPHERD: I understand that. But I also understand that you have no information as to what your average in-service date is in the year, right? I asked you and you said you haven't looked at that.

MS. YOUNG: No.

MR. SHEPHERD: So you have no basis to say six months is a good approximation of monthly in-service, right?

MR. MACDONALD: Only -- only you know the filing requirements and other guidance from the Board. We don't have a -- intrinsic to PowerStream, we don't have analysis. That's correct, Mr. Shepherd.

MR. SHEPHERD: Let me turn to the interest rate on the shareholders' notes. You have about -- what's the total? About 170 million?

MS. YOUNG: Yes. 166 million, yes.

MR. SHEPHERD: Sorry?

MS. YOUNG: 166 million.

MR. SHEPHERD: 166 million of notes to the -- held by the three cities.

And so I am looking at this package that you filed on October 12th, which I guess is entitled "Responses to Undertakings" and it is a 55-page document.

So I want to start with -- I will start with -- on page 1, this is one of the notes. This is the Barrie note, right?

MS. YOUNG: Yes.

MR. SHEPHERD: And as you pointed out, the original

interest rate, if you see at No. 2.1 -- was 6.5 percent?
MS. YOUNG: That's correct.
MR. SHEPHERD: In -- what was it, 2000?
MS. YOUNG: I believe these were actually --
MR. SHEPHERD: This is dated 2008.
MS. YOUNG: Yes. So we had an original promissory note. When Barrie Hydro Distribution Company was first incorporated, it was first formed, we had a promissory note.
This is really an amendment to that promissory note, to change -- we had six and a half percent for the first year, and then there is a clause in there that all shareholders -- that the rate could change, all shareholders of the successor to the corporation.
So it was agreed upon at that time they would get 6.5 for a year, and that they would go to the 5.58, which is the same as Markham and Vaughan.
MR. SHEPHERD: That is not actually what this says, right?
MS. YOUNG: This is not specific in this document. I think it was perhaps the shareholder agreement that specified that, to align all the rates.
MR. SHEPHERD: What it says is that the city and the lender can, in effect, renegotiate the interest rate, taking into consideration market conditions, the OEB's prescribed interest rate and the interest rate on other debt to shareholders; isn't that right?
MS. YOUNG: It specifies in that in 2.1, and then of

course 2.3 talks about the subordination, and that is -- and currently, we have subordination agreements with our three shareholders.

MR. SHEPHERD: Yes. Okay. Sorry, interest rate first, then callability. So let me first deal with interest rate.

MS. YOUNG: Sure.

MR. SHEPHERD: So the 6.5 percent is now 5.8 percent because -- 5.58 percent because the shareholders have agreed they will all get the same rate, right?

MS. YOUNG: Yes. That's correct.

MR. SHEPHERD: And that rate was set in 2010?

MS. YOUNG: Yes. That's correct.

MR. SHEPHERD: And now what was the Board's rate, the Board's prescribed interest rate at that time? Was it 5.58?

MS. YOUNG: In 2010?

MR. SHEPHERD: Yes.

MS. YOUNG: No, I don't believe it was. I don't offhand know what the rate is for 2010.

MR. MACDONALD: I don't have the rate for 2010.

MS. YOUNG: We looked at this as a continuity of the old promissory note, so...

MR. MACDONALD: Remember, 2009, because of rebasing, it was 6.7 percent, I think. I don't recall 2010.

MR. SHEPHERD: See, the reason I ask this is because it says here that when you are resetting the interest rate, you consider what the other shareholders are being paid, but also the OEB's prescribed interest rate.

Did you not do that?

MS. YOUNG: I think that that clause specifically was in there just for this certain circumstance, in that we're a regulated company and that we have to go to the regulator, and that -- that there might be instances where that might change.

I don't think that was meant that -- and it doesn't have any reference to the deemed long-term interest rate.

It was just that we have a regulator and are required to follow -- follow those -- the rulings of the regulator.

MR. SHEPHERD: That is not what it says, right? It says the interest rate will be reset and adjusted from time to time on these three category –- characteristics; isn't that right?

MS. YOUNG: Yes, it does say that.

MR. SHEPHERD: But you didn't look at current market conditions and you didn't look at the deemed interest rate. You only looked at what rate was being paid to the other shareholders?

MS. YOUNG: At the time, we looked at it as non-callable, so we looked at it as long-term debt.

And so we believed that the 5.58 percent -- or in this case, the City of Barrie, the 6.5 percent -- was the true amount of interest that should be charged.

MR. SHEPHERD: Well, the interest rate was set in 2010, right?

MS. YOUNG: The interest rate was changed in 2010.

The shareholders' note had existed. It was amended for an agreement between the three shareholders.

MR. SHEPHERD: Again, I am trying to be fairly precise here. The interest rate of 5.58 of this note was set in 2010?

MS. YOUNG: Yes, that's correct.

MR. SHEPHERD: And at that time, was that the market interest rate? Because I remember in 2010 it was not.

MS. YOUNG: No. That 5.58 percent was to align with the other two shareholders.

MR. SHEPHERD: All right. So -- and then you said that this promissory note -- and I am going to get to the other ones in a second, but this promissory note has a subordination clause that says that the lender will subordinate to EDFIN, first of all, right?

MS. YOUNG: Yes.

MR. SHEPHERD: EDFIN is gone now?

MS. YOUNG: That's correct.

MR. SHEPHERD: So that is not relevant anymore, right?

MS. YOUNG: Yes. 4.1 mentions EDFIN, and then 4.2 goes on to talk about other debt issued by the corporation and financial institutions. So it is the 4.2, the requirement.

MR. SHEPHERD: Okay. So when did Barrie subordinate to third-party debt?

MS. YOUNG: Barrie had always been subordinated in the -- under the EDFIN agreement, and then now --

MR. SHEPHERD: Okay. But that is gone now, right?

MS. YOUNG: And then now were asked to subordinate for a $200 million private debt issue.

MR. SHEPHERD: That is in August 2012?

MS. YOUNG: Yeah. So there's a -- it is basically seamless. Up to August 2012 you had EDFIN, and then that was replaced by a $200 million debt issue.

MR. SHEPHERD: How much was EDFIN?

MS. YOUNG: 125, I believe. Yes, 125.

MR. SHEPHERD: If you could move to page 5 of this, this is the note from -- to Markham. The notes to Markham and Richmond Hill are the same, right? Or Vaughan, rather?

MS. YOUNG: Yes, that's correct.

MR. SHEPHERD: They just have different dollar principal amounts, but the terms are identical?

MS. YOUNG: That's correct.

MR. SHEPHERD: Okay. So your interest rate is 5.58 percent, but in 2.4, you will see it says it will be adjusted to reflect market conditions and the deemed interest rates as prescribed by the Ontario Energy Board.

Has that ever been done?

MS. YOUNG: No.

MR. SHEPHERD: Okay. So now I want to go to the postponement agreement, and that starts on page 11. And this was signed in counterparts, right?

MS. YOUNG: Sorry?

MR. SHEPHERD: It was signed in counterparts. Not everybody signed the same document?

MS. YOUNG: That's correct.

MR. SHEPHERD: So the first thing I want to ask you is, has everybody signed this, because we didn't have all signatures in this package. Has everybody signed this agreement?

MS. YOUNG: Yes, they have.

MR. SHEPHERD: And when did everybody sign it?

MS. YOUNG: I believe there's three copies and under each, either town or city, the signatures are on there.

So it looks like -- I see a signature right now from the mayor of Markham, and the date is June 26, 2012.

MR. SHEPHERD: Okay, I understand that. But see all of these signatures aren't here. There are signatures not in this package, and that is why I am asking. At what point did you have all of the signatures?

MS. YOUNG: Well, I think there is three copies. I believe their signatures -- each one has signed their own agreement.

And so the next one will have the town – sorry, the City of Vaughan, the next one will have the City of Barrie. I believe all of the signatures are there. But they have definitely all been signed.

MR. SHEPHERD: Okay. I am asking when that was, because so far I have Barrie, Markham --

MS. YOUNG: Vaughan is on 40 of 55.

MR. SHEPHERD: Yes.

MS. YOUNG: And was signed June 26, 2012.

MR. SHEPHERD: So I don't have PowerStream or Computer Share.

MS. YOUNG: Oh, so you're saying the other parties?

MR. SHEPHERD: All of the parties have to sign for it to be a binding agreement, right.

MS. YOUNG: Yes. Yes, it isn't indicated here, but yes all of the parties have signed.

MR. SHEPHERD: And they would have signed on June 26 or 27, somewhere around there?

MS. YOUNG: That's correct.

MR. SHEPHERD: Okay. So at that point, this was then a binding postponement agreement, right?

MS. YOUNG: That's correct.

MR. SHEPHERD: And until that time, the -- you're saying there was a postponement agreement with EDFIN?

MS. YOUNG: That is correct.

MR. SHEPHERD: Is that in the evidence?

MS. YOUNG: I do not believe it is.

MR. SHEPHERD: Okay. When is it dated?

MS. YOUNG: The -- specifically the postponement agreements? I think EDFIN started in 2002. Is that -- I will have to confer with my colleagues.

MR. SHEPHERD: Well, no, the postponement agreement wouldn't have been then, though, because these were later, right? Some of these notes were later.

MS. YOUNG: Yes. So with EDFIN, EDFIN was set up, I believe -- I think it was early 2000, and we would have gotten postponement agreements. You know, Barrie Hydro would have been separated from Vaughan and Markham, but they would have signed those agreements previously.

MR. SHEPHERD: So can you file the postponement agreements -- you are relying on those postponement agreements for subordination prior to June of this year, right?

MS. YOUNG: That's correct.

MR. SHEPHERD: So can you file the ones you are relying on then, please?

MS. YOUNG: Certainly.

MS. SEBALJ: J1.5.

UNDERTAKING NO. J1.5: TO FILE POSTPONEMENT AGREEMENTS FOR SUBORDINATION RELIED UPON

MR. SHEPHERD: And so -- right now, we know that PowerStream can borrow on the market at 3.99 percent or maybe less even now. But certainly you just recently borrowed at 3.99 percent, right?

MS. YOUNG: Yes, that's correct.

MR. SHEPHERD: When these shareholders locked in the 5.58 in June, you were actually able to borrow at that rate, weren't you? At 3.99?

MS. YOUNG: June? Yes, that's correct. Part of our -- if I may, a part of the rate that we get is they require these subordination agreements and postponement agreements.

So because they're subordinated debt, which means from a legal point of view, they have the lowest priority in the debt sequence, that helps us get favourable rates with our -- from rating agencies and from the market in general. So there is advantages to having that subordinated debt.

MR. SHEPHERD: Understood. So you did an analysis of what the fair interest rate was on that debt, that $166 million in debt, in June?

MS. YOUNG: Well, no. I believe as a company we treat it as long-term debt, and I believe the Board allowed the rate that was set up originally on the promissory note.

So at that time, we did not look at a different interest rate. We looked at it as long-term debt, a 20-year debt due May 31, 2024, and accordingly, kept it at the rate of 5.58 percent.

MR. SHEPHERD: It's -- the 5.58 is a rate from some years ago. Presumably, you could borrow at a different rate, a lower rate, that $166 million today?

MS. YOUNG: Well, I guess now that we have a subordination agreement and – sorry, I’ll call it a postponement agreement, I think -- I believe, unless we get permission from the trustee, we have to pay off that $200 million debenture, which I believe would be millions in interest and penalties to be able to do that.

So I don't believe that we can -- call that $166 million.

MR. SHEPHERD: Did you look at -- but my question is not can you do it today. My question is, could you do it in June. You could, right? You could have financed 366 instead of 200; you didn't.

MS. YOUNG: Yes, I guess we could have. I mean, the - we didn't look at it as - we liked the fact of having long-term debt and subordinated debt, and again it helps us in the market with a favourable rate.

So, no, we didn't look at it at the time.

Mr. Macdonald is just explaining to me in the agreements that -- I guess we can't make the decision. They're not redeemable; it’s a callability, so that we really can't make the decision to call them on the $166 million debt.

So I guess it would have to be the shareholders who request, not us, who request to pay off the $166 million.

MR. SHEPHERD: So you can't repay this loan if interest rates go down?

MS. YOUNG: That is correct.

MR. SHEPHERD: Where does it say that?

MS. YOUNG: I will confer -- to Mr. Macdonald.

[Witness panel confers]

As I understand the agreements are -- there's not a specific note that says that they are redeemable or not redeemable.

So the issue here is they would not be redeemable, but they are -- it's the question of callability.

So I guess it’s the absence of the right of PowerStream to redeem them.

MR. SHEPHERD: You're saying as a matter of law, if the note doesn't say whether you can pay it off early, then you can't?

MS. YOUNG: I believe so.

MR. SIDLOFSKY: Mr. Chair, I am not sure Ms. Young is in the best opinion to give a legal opinion here. I don't think she should be asked for one. I think she could be asked for her understanding of it, but not to opine as a matter of law on the meaning of the note.

MR. SHEPHERD: I am only asking for her understanding as to why they can’t be repaid.

MS. YOUNG: Yes. My understanding -- as I am conferring with Mr. Macdonald, that it doesn't specify in the agreement that it is redeemable. So I guess as a company, we do not believe that we have the right.

MR. SHEPHERD: At the time you did this financing in June -- actually the financing, I guess, was in August, right?

MS. YOUNG: That's correct.

MR. SHEPHERD: But you did the postponement in June?

MS. YOUNG: Yes, it was --

MR. SHEPHERD: But that was just one of the documents you were preparing as part of the closing in August?

MS. YOUNG: Yes, it was important the trustee that we have that -- those documents in place.

MR. SHEPHERD: So they didn't actually become effective until August, because you didn't have a debt to postpone to until August.

MS. YOUNG: The debt for the EDFIN would have been up to the end of August, you're right.

So that agreement would have -- would have had it not callable, and then it is transferred to the $200 million debt. Yes.

MR. SHEPHERD: Well, actually, I guess, unless this trust indenture that you are referring to on June 27th, 2012 is the EDFIN document -- it's not, right?

MS. YOUNG: Sorry, no. That is the $200 million -- the postponement agreement is the $200 million private placement, yes.

MR. SHEPHERD: Which actually happened in August?

MS. YOUNG: In August.

MR. SHEPHERD: You closed in August, but your paperwork was done in June?

MS. YOUNG: That's correct.

MR. SHEPHERD: Yeah, okay.

MS. YOUNG: And EDFIN continued until August, so it was basically --

MR. SHEPHERD: So at the time you did this, did you talk to the cities about whether they should get a lower interest rate, based on market conditions? Or alternatively, that you would like to pay them out and get cheaper money?

MR. MACDONALD: No, we did not.

MR. SHEPHERD: Why not?

MR. MACDONALD: We set our course to refinance the EDFIN debt, which was coming due, and add some other debt to that, some short-term debt that we had. We would have had to have effectively asked them to call their debt, and we did not -- we did not pursue that discussion with our shareholders.

MR. SHEPHERD: Well, there was a negotiation that went on anyway, right? Because they had to sign these postponement agreements, right?

So you negotiated that right there and then, right? Because otherwise, you couldn't raise the 200 million?

MR. MACDONALD: Well, there really was not a lot of discussion. It was something they were prepared to do because it was required -- a condition of the -- the trustee for the new debt.

We did not -- we did not, like, develop a strategy with our shareholders about disposing of their debt at all, did not -- didn't have that discussion with them.

MR. SHEPHERD: They given you no indication that they wanted this debt to be repaid?

MR. MACDONALD: No, they -- agreed. They treated it as long-term debt, and they don't -- they have never indicated to us that they plan to call it.

MR. SHEPHERD: Okay. I think that is all of my questions.

Thank you, Mr. Chair.

MS. SEBALJ: I think I am the only remaining party who has questions for this witness panel.

MR. QUESNELLE: Is that it for you, Mr. Shepherd? Thank you. Thank you, Mr. Shepherd.

MS. SEBALJ: I did prepare a compendium. It is not tabbed, but there is not very much in it, so I can...

[Ms. Sebalj passes out compendium.]

CROSS-EXAMINATION BY MS. SEBALJ:

MS. SEBALJ: This is just for convenience. There is nothing in here that isn't otherwise in the evidence, except for the first document at the front, which is the addendum to the Report of the Board on the Implementation of IFRS in an Incentive Rate Mechanism Environment, which I think all of the parties are familiar with.

That is where I will start. The only questions I have remaining as a result of the cross that has occurred are related to the PP&E account issue.

And with respect to the report -- I think you referred to this in your chief -- but PowerStream participated in the working group that led up to the formulation of this report, did it not?

MR. MACDONALD: Yes. Mr. Barrett was on the working group.

MS. SEBALJ: And that -- the work of that group culminated in a Board Staff discussion paper, which was ultimately considered by the Board in the development of this report; is that correct?

MR. BARRETT: That's correct.

MR. MACDONALD: Yes.

MS. SEBALJ: If we turn to page 2 of the report, it says there the Board believes –- sorry, I think it is the first full paragraph.

It says:

> "The Board believes that the 2009 Report of the Board as amended in this addendum and the depreciation study referred to above provide the guidance necessary for distributors to implement IFRS effective January 1, 2012 in the Ontario regulatory environment."

So to my knowledge, there is nothing else that provides guidance with respect to the issue that we're looking at, other than the documents that are referred to there; is that correct?

MR. MACDONALD: I believe that is correct, yes.

MS. SEBALJ: And the issue is outlined at page 9, and at the top of page 9 it says "Issue 2."

This, of course, is excerpted from the Staff discussion paper, so the definition of the issue was provided from the Staff discussion paper.

It says:

"Should any differences between costs recorded in the balance sheet accounts and costs built into rates that..."

Bullet 1:

"... arise in the time period between rebasing and CGAAP and the first rebasing under MIFRS."

And bullet:

"... are driven by changes in accounting for capital or operating costs prompted by the adoption of MIFRS be recovered from or refunded to ratepayers? If yes, on what basis?"

And then it goes on to say:

"The Staff proposal on this issue read as follows: 'Staff proposes that differences relating only to the property, plant and equipment components of rate base, including the rate base-related intangible assets, referred to

collectively hereafter as PP&E, when properly
calculated should be recoverable from or
refundable to ratepayers.'"

Is that correct? That's what it says?

MR. MACDONALD: Yes.

MS. SEBALJ: And would you agree with me that, from a regulatory perspective, assets in rate base are those that are used and useful?

MR. MACDONALD: For ratemaking, yes.

MS. SEBALJ: Okay. For instance, assets in inventory are not in rate base?

MR. MACDONALD: Yes.

MS. SEBALJ: And in general, CWIP is not in rate base?

MR. MACDONALD: For ratemaking, yes.

MS. SEBALJ: And for the purpose -- with respect to the capitalization policy, you would agree with me that the Board went on to accept -- sorry, not the capitalization policy. With respect to the policy on PP&E, you would agree with me that the Board went on to accept Staff's proposal?

On page 11 of the report, under the heading "PP&E Account," the second full paragraph says:

"The Board will approve the proposed PP&E
deferral account."

And then in the next paragraph, it says:

"The Board therefore authorizes a generic
deferral account to capture PP&E differences
arising only as a result of the accounting policy

changes caused by the transition from CGAAP to MIFRS."

I believe if you flip to the next page, it says:

"The operation of the deferral account is based on the Staff proposal and set out in detail in appendix A."

Appendix A essentially reproduces the five -- the five components of the mechanism for recovery which Staff recommends, on pages 9 and 10.

So ultimately the Board accepted Staff's proposal in this regard; do you agree with me?

MR. MACDONALD: Yes.

MS. SEBALJ: And this obviously created deferral account 1575, which is the PP&E account that we've been talking about.

And if we would turn for a moment to the settlement proposal -- which isn't in your package, because I assumed that everyone would have it with them today -- at page 28 of 32, that is where we talk about this Issue 8.2 which is unsettled. It says:

"PowerStream has included the difference in overheads capitalized between CGAAP and MIFRS on both rate base and CWIP as of the end of 2012 in the calculation of the amount to be recorded in Account 1575, IFRS/CGAAP transitional PP&E amounts."

And then of course it goes on to say that it needs to be brought to the Board for resolution.

So just to be very clear, PowerStream has included CWIP up to the end of 2012 in the PP&E deferral account?

MR. BARRETT: I think it would be more accurate to say that we have included the differential in overhead that would have been capitalized in 2012, that is still remaining in WIP at the end of 2012.

MS. SEBALJ: Okay. And I think -- I think earlier when you were speaking to Mr. Shepherd, there was -- at least I got confused, because there was some discussion about 2011. But we're talking about 2012 in this, 2012 amounts, correct?

MR. BARRETT: It is because of the alternative method would cut off rate base at December 31, 2012, would ignore the difference between the WIP that would have gone in -- that would be Canadian rate base, or Canadian GAAP rate base in 2013.

MS. SEBALJ: Right.

MR. BARRETT: Does that help?

MS. SEBALJ: Yes, yes.

MR. BARRETT: Okay.

MS. SEBALJ: So if we flip to the next piece in the compendium, it should be right after the stapled report, there is appendix 2-EA, which is of course an appendix to the revenue requirement work form.

And just so that I can put some numbers to this for Staff's purposes, and for the benefit of the Panel, my understanding is that this table shows the difference between IFRS and CGAAP amounts recorded in the PP&E deferral account. Is that correct?

MR. BARRETT: That's correct.

MS. SEBALJ: And to be clear, the numbers in this table include CWIP and the PP&E values for both CGAAP and MIFRS, correct?

MR. BARRETT: That's correct.

MS. SEBALJ: Can you just take us through the table as a starting point? So the first four rows are showing PP&E values under CGAAP under 2011 and 2012 years, is that right?

MR. BARRETT: That's right, hmm-hmm.

MS. SEBALJ: Then the next four rows are PP&E values under MIFRS, 2011/2012.

MR. BARRETT: Hmm-hmm.

MS. SEBALJ: And then according to this appendix, the total difference between CGAAP and IFRS PP&E amounts is -- the rows aren't numbered, but it is, it's a refund, so it is a negative number, 2,575,585, is that correct?

MR. BARRETT: No. There is a further adjustment down below that brings it to the two-million-386 --

MS. SEBALJ: Okay. That is what I was going to take you through, but -- so that is the sub total, and then the adjustments are as a result of -- this is the Aurora adjustment?

MR. BARRETT: Yes. These other numbers were prepared by our accounting, and they have the Aurora fair market value bump in their numbers, so we have to take it out.

MS. SEBALJ: So the amount that PowerStream is asking to put into the deferral account is 2,386,855?

MR. BARRETT: Correct.

MS. SEBALJ: Amortized over four years, which brings you to 596,714?

MR. BARRETT: Correct.

MS. SEBALJ: And that -- just as a small pause here, I notice that the return on rate base associated with the PP&E balance at weighted average cost of capital is not included in this appendix.

Can you explain why that is?

MR. BARRETT: We didn't do the calculation here. We did the calculation in calculation in calculating our rate base. In our rate-base calculation, we have adjusted it to remove the roughly $2.4 million dollars.

MS. SEBALJ: And when you say in rate base, that is in your revenue requirement work form, that is the 802 million number for fixed assets?

MR. BARRETT: Correct. We have deducted the 2.4 million in arriving at the rate base amount to calculate revenue requirement.

MS. SEBALJ: Thanks. So now – sorry, I included -- the next appendix you will see is 2-CD, and that was just to show that at the very bottom, the second-to-last number, the 596,714, finds its way into the depreciation and amortization expense table. And that is the number taken from 2-EA, correct?

MR. BARRETT: That's correct.

MS. SEBALJ: So the next piece in your package, panel, is a filing made October 1, 2012, which was undertakings arising out of the technical conference.

This is only the excerpt relating to an undertaking JT1.4, and that was based on a request by Mr. Aiken that PowerStream provide a version of the appendix using the fixed asset amounts from appendix 2-B, which is -- it is fixed asset amounts.

And you will see from the actual verbiage in the response that PowerStream -- and I think this is what you were referring to earlier, Mr. Macdonald. PowerStream, while it was preparing it in accordance with the request of Mr. Aiken, didn't agree with it.

MR. MACDONALD: That's correct.

MS. SEBALJ: But if we turn to that one, essentially this table now shows the same -- it has the same look as the other table. So it is 2-EA revised, it is called.

And we look at the PP&E values under CGAAP, those four columns, PP&E values under MIFRS, and then the difference now is this 9,571,000 number, is that correct?

MR. BARRETT: I don't have it in my bundle.

MS. SEBALJ: Oh, you're kidding? I'm so sorry.

MR. MACDONALD: I will share mine.

MR. BARRETT: Yes, correct.

MR. MACDONALD: Yes, that's correct.

MS. SEBALJ: And so this is the effect of not including CWIP in the PP&E deferral account?

MR. BARRETT: Correct.

MS. SEBALJ: Correct. Oh, and the amortized amount is the 2,392,750. So it would be basically 2.4 million, I think is what you called it, Mr. Macdonald, this morning, per year, refunded to ratepayers?

MR. MACDONALD: No. Just to be clear, I had talked about the $2.4 million from the schedule we just showed, and that would be the $600,000 refund over four years, in each of four years. This is taking a higher number and dividing it by four.

MS. SEBALJ: Right. Sorry.

MR. MACDONALD: They're not the same number.

MS. SEBALJ: No, they're not the same number. Your proposal is to refund the 691 per year. This is --

MR. MACDONALD: Much higher number.

MS. SEBALJ: -- the impact of not including CWIP in the PP&E account?

MR. MACDONALD: That's correct.

MS. SEBALJ: And I assume, if the Board ordered PowerStream to provide -- to base the calculation in the way that Mr. Aiken has structured it, that the -- there would be a change as a result of a WAC adjustment as well? It is a different set of numbers.

MR. BARRETT: Our understanding is that is the methodology, is that you adjust both your rate base for this amount, and then you amortize it over a number of years. We followed the default of four years although, if you accept it longer, you might possibly be adjusting rate base in a future cost of service as well.

So, yes, my understanding is the methodology from the report is you adjust rate base, and then you amortize it, and you continue to adjust your rate base until it is fully amortized. You amortize it by reducing the depreciation as shown in both of the 2-EA schedules.

MS. SEBALJ: And so the $7 million, or the $7.2 million that you were discussing this morning is the delta between this -- the $9.6 million and the $2.4 million dollar amounts?

MR. MACDONALD: That's correct.

MS. SEBALJ: Then the next in the series of documents is a clarification, I will call it. I am not sure -- I want to be fair. I can't recall what PowerStream called it – yes, further clarification regarding PowerStream's calculation of account 1575.

So this is a filing made October 12, so it is the same -- I have just excerpted it, but the same package of documents that included the promissory notes and postponement agreements we were just looking at.

And so in this clarification, PowerStream essentially laid out its position on the issue, and then provided further tables in the last page of that, which essentially provide a summary of the discussion and highlight the -- the difference that I just spoke about.

MR. MACDONALD: Yes. So Ms. Sebalj, there is no -- there's no new information here. It was an attempt to solidify things and condense information.

MS. SEBALJ: Okay. And the difference in this table is the 7.184 million, is that correct?

MR. MACDONALD: It's the same number again, yes, that's correct.

MS. SEBALJ: Okay. And if you just look now in your package to appendix 2-U, this table shows PowerStream's one time IFRS transition costs, is that correct?

MR. MACDONALD: Yes.

MS. SEBALJ: And am I reading it correctly when I say that the Board-approved IFRS transition costs funded through rates in the 2009 cost of service of 2-million-29 dollars? 29,000?

MR. MACDONALD: No. I would say "no". Actually, in 2009, we had put our transition costs in rates; you know, the cost to do the project.

But we – well, not just PowerStream, but [inaudible] got direction later to use -- for those who had done that, to use a deferral account. So that deferral account is actually being cleared, if I am correct, as part of this application.

MR. BARRETT: That's correct.

MR. MACDONALD: So actually in effect that was settled, the clearance of these amounts.

MS. SEBALJ: Sorry. I am not raising it as an issue that is not settled. I am just raising it to understand how much money PowerStream has spent and is asking for approval on IFRS transition costs.

And it is in the $2 million range; is that correct?

MR. MACDONALD: That's correct.
MS. SEBALJ: Most of that was for professional accounting fees? Or a big chunk of that?
MR. MACDONALD: That's correct. I would say most was for professional accounting fees, but our approach was to put some of our stronger staff on the project and we back-filled. So there was a second component of having contract staff in certain positions.
But you are correct; it's mostly experts in the area that we hired.
MS. SEBALJ: You hired KPMG?
MR. MACDONALD: That's correct.
MS. SEBALJ: As your -- I know there were a number of firms mentioned in your evidence, but KPMG was the lead accounting firm?
MR. MACDONALD: Yes. Yes, that's correct.
MS. SEBALJ: When were they retained?
MR. MACDONALD: I am looking for help from my panel. I am going to say 2008. I just --
MS. SEBALJ: I think that is right. I am not testing you. I'm just -- I didn't write it down.
MR. MACDONALD: That's right, because we had an amount for 2009 EDR, so 2008. Yes, that would be right.
MS. SEBALJ: And as I understand from your evidence -- and this is your evidence at A3, tab 1, schedule five - which is international financial reporting standards, that you, PowerStream itself, had been looking at IFRS transition before 2008? You started a multi-disciplinary

team?

MR. MACDONALD: Yes.

MS. SEBALJ: I am trying he can to recall when, but it was before you hired KPMG, obviously?

MR. MACDONALD: Yes. We tried to get ahead of the issue.

MS. SEBALJ: And that multi-disciplinary team, in accordance with your evidence, consisted of finance, accounting, rates and regulatory, engineering, information systems and internal audit, is that correct?

MR. MACDONALD: Yes.

MS. SEBALJ: And would you agree with me that one of the issues that arose for other organizations transitioning from CGAAP to IFRS was related to the way IFRS treats capitalization of PP&E? So other organizations including your own? And in particular, that one can capitalize less of the overheads under IFRS, and should expense them under IFRS?

MR. MACDONALD: Yes. Very much so.

MS. SEBALJ: And in that regard, can you tell me at what point in time PowerStream became aware of that issue?

MR. MACDONALD: I am just going from memory, but we started doing some modelling in 2010 and '11 of the -- I mentioned this in my earlier remarks -- the quantum of the burdens that couldn't be capitalized and went to OM&A.

And there was an offsetting amount, lower depreciation, because of the asset life study.

So I think we started to do some modelling of that in

-- I don't think we do did it during our cost of service year. I think we did it in 2010 and '11, did some modelling of those differences.

MS. SEBALJ: And in particular, this CWIP issue, if I look -- if I look to page 11 of 27 of the exhibit to which I just referred, the A3, tab 1, schedule 5, you have there a table 4, which is a summary of differences between CGAAP and MIFRS.

I don't know if you have that.

MR. MACDONALD: Can Mr. Vetsis call it up?

MS. SEBALJ: It is Exhibit A3, tab 1, schedule 5. No, this is their evidence.

MR. MACDONALD: In the original application?

MS. SEBALJ: Yes.

MR. MACDONALD: So it is an A exhibit?

MS. SEBALJ: It is an A, A3-1-5.

I guess just -- sorry, before I go to the table I was just talking about, there is a -- page 4, I think, if I am right in my notes, page 4 of 27, starting at line 6, it says:

"PowerStream's IFRS project consisted of four phases, initial assessment, detailed assessment, design and implementation. PowerStream completed its initial assessment in 2008, and detailed assessment during the first quarter of 2009, which involved a high-level review of the major differences between CGAAP and IFRS. During the detailed assessment, it was determined that the area of accounting differences with the highest potential impact to PowerStream would be the accounting for property, plant and equipment. PowerStream developed a detailed project plan for the impacted areas to determine the IFRS options, business process changes and system changes."

So would it be fair, then, to say that you were aware of this CWIP issue in the first quarter of 2009?

MR. MACDONALD: No. I think this refers to PP&E in totality.

MS. SEBALJ: Okay.

MR. MACDONALD: We really didn't dwell on CWIP, and actually Mr. Barrett can help, but I am not sure the working group in the paper you referred to earlier, Ms. Sebalj, really -- really nailed that one.

MS. SEBALJ: That's correct.

MR. MACDONALD: So do you want to add to that or not?

MS. SEBALJ: No, the paper I referred to, I think I have the dates here. The Board Staff discussion paper was on March 31st, 2011, and the report itself is dated June 13th, 2011.

MR. MACDONALD: I think it is quite fair to say that the issue we have today that is unsettled, that really only emerged during this proceeding. That is not something I remember -- I was quite involved in this project at PowerStream from a regulatory point of view. I don't remember flashing lights coming on to do with CWIP, ever.

MS. SEBALJ: And given the magnitude of the delta, why is that, that either PowerStream or KPMG didn't see this?

MR. MACDONALD: You know, I have a feeling what it is is -- you made the comment about CWIP being part of rate base or not.

I think that is what -- maybe what has happened here is -- CWIP is not part of rate base, but that is not what is happening here. This is an accounting change, and that is where -- that's why it gets stuck or stranded, so...

MR. BARRETT: I might put that a different way. I would say CWIP is not rate base at any point in time; it's rate base to come. It is future rate base.

So we haven't included anything in WIP in these numbers that isn't going to be rate base. If you pick an arbitrary point in time, such as December 31st, 2012, it is not rate base yet.

MS. SEBALJ: But CWIP is not rate base yet. It doesn't go into rate base; it is CWIP?

MR. BARRETT: No, it goes into rate base. It goes into rate base. The difference isn't that CWIP isn't going into rate base. The difference is that 2012 -- sorry?

Yes, so the difference isn't that it is not going into rate base; the difference, the issue here is that there are different amounts of Canadian CWIP, a higher amount, shown actually on this last document we were referring to in your handout here. If you look at table JT1.4-2, the second -- the second line from the bottom, you will see there are two very different amounts of CWIP at December 31st, 2012.

Under Canadian GAAP, there is a little over

37 million. Under IFRS, there is 29.9 million.

The difference isn't that they're not both going in. Both of those numbers would go into rate base. Under Canadian GAAP rate base, the 37.1 million would go into rate base in 2013. Under IFRS, the 29.9 million is what is going into rate base in 2013.

The difference of 7.2 million that is expensed under IFRS but capitalized under Canadian GAAP is lost because of the switch from Canadian GAAP rate base to IFRS rate base, and we do not believe that was the intention of the report or even what the report says. The report talks about continuity of rate base.

MS. SEBALJ: Right. I mean, that will be a matter for argument, but, you know, I can take you to quotes in the report that clearly refer to rate base, and you will take me to the sentence that says that utilities are to be kept whole. So we don't want to have that debate here.

MR. BARRETT: But clearly that is what is happening. It is not that CWIP doesn't go into rate base; it is that under Canadian GAAP a higher amount would go into rate base, and under IFRS a lower amount goes into rate base.

That is the issue.

MS. SEBALJ: And I understand the issue. I guess the question is whether the PP&E account created by this Board, 1575, was intended to capture that $7 million delta or not.

And to that end, I wanted to ask whether PowerStream is aware that a number of utilities have identified issues analogous to this one, though not identical; in other words, issues arising out of the accounting treatment differences, the transition from CGAAP to another accounting -- in most cases in the other utilities it was transitioned to US GAAP, where they said there would be a negative -- a significant negative impact on shareholder equity because of out-of-period costs.

But they came to the Board in advance and asked for specific deferral accounts to be established to address these issues.

MR. MACDONALD: So we did not do that. As I stated earlier, we really thought and we still do that we did the accounting for that deferral account properly.

This really only arose at the technical conference in September, where the alternate view was presented, and we disagree with that view, strongly.

MS. SEBALJ: Is it not the case that when PowerStream became aware of the potential out-of-period costs that it could have adjusted its capitalization policy to mitigate the impact that it is now seeing, this $7 million?

MR. BARRETT: No. I don't believe that is the case. Under Canadian GAAP, we have one set of accounting and that is consistent with what -- how rates are set. Under modified IFRS, we've worked with our consultants and come up with what is permitted under IFRS.

I don't –- I'm not sure what we could have done differently there.

MS. SEBALJ: All right. Those are all of my questions. Thanks.

MR. QUESNELLE: Thank you, Ms. Sebalj.

Mr. Sidlofsky, any redirect?

MR. SIDLOFSKY: Just a few questions, sir, if I might.

RE-EXAMINATION BY MR. SIDLOFSKY:

MR. SIDLOFSKY: I am going to start, panel, with my friend Ms. Sebalj's questions.

She had suggested that some of these issues are likely better addressed in argument, but I am going to ask you, just relating to Ms. Sebalj's exchange with you, about CWIP being a part of rate base.

If I could take you to the Board's addendum to the report on implementing IFRS, and it's to an area on page 11 that Ms. Sebalj actually did refer to. And the paragraph begins:

> "The Board will approve the proposed PP&E deferral account. The account addresses the unique circumstances of a change in accounting standards and provides for the continuity of rate base."

And Ms. Sebalj also mentioned to you, panel, that the Board adopted the Staff approach. Specifically, the Board said:

> "The operation of the deferral account is based on the Staff proposal and is set out in detail in appendix A."

That is on page 12 that report.

Either Mr. Barrett or Mr. Macdonald, could you tell me, first of all, is this a rate base issue for you? Perhaps Mr. Barrett; do you see this as an issue related to rate base?

MR. BARRETT: I see it as an issue related to the statement in the paragraph you just read, where it says, "provides for continuity of rate base" but it is more than just rate base.

The report also goes on to say that the purpose is also to avoid the potential for material out-of-period costs.

And certainly the interpretation in the alternative would create a very significant, very material out-of-period cost.

It's our understanding that the whole purpose of the PP&E deferral account was to allow that continuity of rate base, which would include the amounts that would be capitalized under Canadian GAAP in 2012, expensed under IFRS, to go into rate base before we adopt a modified IFRS rate base.

I would also believe that the purpose was to avoid having that 7.2 million being out-of-period cost.

MR. SIDLOFSKY: Thank you, Mr. Barrett.

Just going back to a couple of Mr. Shepherd's questions, first of all, Ms. Young, Mr. Shepherd took you to section 2.4 of the Markham -- the Town, now City of Markham note.

That was from your October 12th filing, I believe?

MS. YOUNG: Yes.

MR. SIDLOFSKY: Is that correct? I am just hoping you can clarify one thing for me.

I believe Mr. Shepherd asked you about section 2.4 of that note, and he suggested to you that it said that the rate will be adjusted from time to time to reflect current market conditions and the Board's deemed interest rate.

That is not exactly what that note says, is it, in section 2.4?

MS. YOUNG: Well, I can read the actual section.

MR. SIDLOFSKY: Does it say it will be adjusted? That is really my question.

MS. YOUNG: No:

> "It may be adjusted from time to time, as agreeable between the Town and Amalco..."

Which is now PowerStream.

> "...in order to reflect current market conditions and the deemed interest rate as prescribed by the Ontario Energy Board."

MR. SIDLOFSKY: So that note doesn't require an adjustment; is that right? There is no requirement for an adjustment in that note?

MS. YOUNG: No, no. That's correct. And in fact, there has never been an adjustment to the 5.58.

MR. SIDLOFSKY: Okay. And Mr. Shepherd was also talking to you about the timing of the postponement agreement and the subordination or the -- well, the postponement agreement, sorry, in relation to the new debt that was issued in August.

You recall that exchange, I imagine?

MS. YOUNG: Yes, I do.

MR. SIDLOFSKY: Were there any other postponement agreements in place? I know that in -- maybe the easiest place to take you to is page 24 of the settlement agreement, where you have a table of all of your 2013 test year long-term debt.

MS. YOUNG: Yes.

MR. SIDLOFSKY: The -- there is a bank loan from TD listed. That is item 10 in that table.

MS. YOUNG: Yes. The $50 million --

MR. SIDLOFSKY: That's right. Was there any requirement for a postponement of that?

MS. YOUNG: I believe there was.

MR. SIDLOFSKY: And when was that note -- that loan entered into?

MS. YOUNG: It is right on the --

MR. SIDLOFSKY: It says in the table February of 2008.

MS. YOUNG: That's right.

MR. SIDLOFSKY: For the five-year term?

MS. YOUNG: Yes. And that is due in 2013.

MR. SIDLOFSKY: Okay. Thank you.

I think those are my questions, sir. Thank you very much.

MR. QUESNELLE: Okay. Thank you very much, Mr. Sidlofsky.

PROCEDURAL MATTERS:

One thing that you had mentioned in your opening remarks is the schedule.

The Board certainly accepts that we will have all of the submissions in writing.

We're a little concerned about the length of time that was suggested in laying this out. I would just remind the applicant that they have requested a January 1 date. All things being equal, we would like to keep ahead of that, so that we're not worrying about implementation dates beyond that if we don't have to.

Also, considering the scope and breadth of the unsettled issues, the Board feels that we can probably accelerate on the proposed schedule that you had mentioned at the outset, Mr. Sidlofsky.

Today is Monday. We are wrapping up. We did have three days scheduled; we're obviously not using those.

We would suggest that perhaps, given the scope, that you could have argument in-chief for this Friday.

MR. SIDLOFSKY: The only concern I have, sir, is that there is a number of undertakings that do need to be -- undertaking responses that need to be prepared by PowerStream.

I understand the Board's concern. I am very conscious of that.

I am wondering if -- I mean, given the undertakings, we would suggest that the 7th is appropriate.

If the Board did want to reduce that time somewhat, might I suggest Monday the 5th? That would allow a bit of time for preparation of the undertaking responses, which I am sure the PowerStream people will jump on, but it also allows for a reasonable amount of time for preparation of that argument.

MR. QUESNELLE: Okay. Given that that information is something that will be in your hands, the 5th, I am just looking here, so that would be this coming Monday? Okay.

So we will go with the 5th for argument in-chief, submissions a week later, plus a day. If we went with the 5th through to the – November the 13th, a week and a day.

Mr. Shepherd?

MR. SHEPHERD: Mr. Chairman, I am okay with the 13th. And I can't speak for other intervenors, but it would be of assistance to us if the Board Staff argument was a couple of days earlier. So if the 5th is for in-chief, if Staff can file on the 9th, I think we could file on the 13th, but if the 9th is tight for Staff, then maybe the 12th and the 15th would make more sense.

MR. QUESNELLE: Board Staff?

MS. SEBALJ: That is fine with me.

MR. QUESNELLE: The 9th?

MS. SEBALJ: Yes.

MR. QUESNELLE: Okay. So we will go with the 9th. And then we will go with the 13th for intervenors, which then wraps up with a –- 13th, looking ahead -- 21st for reply.

MR. SHEPHERD: I would have thought the reply could be a lot faster.

[Laughter]

MR. QUESNELLE: That would be on the 13th, the -- I am just looking here. The 21st would be fine for the Board's purposes. We're thinking of the preparation of the -- what has to be done by the Board beyond that date, and we are comfortable with that.

Okay?

MR. SIDLOFSKY: Thank you, sir.

MR. QUESNELLE: Thank you.

Okay. I thank the witness panel. Thank you very much for your forthright responses this morning. Very helpful. Thank you.

And with that, we are adjourned.

--- Whereupon the hearing adjourned at 12:43 p.m.