Hydro One Networks Inc.
7th Floor, South Tower
483 Bay Street
Toronto, Ontario M5G 2P5
www.HydroOne.com

Tel: (416) 345-5700
Fax: (416) 345-5870
Cell: (416) 258-9383
Susan.E.Frank@HydroOne.com

Susan Frank
Vice President and Chief Regulatory Officer
Regulatory Affairs

BY COURIER

April 22, 2014

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

Dear Ms. Walli:

EB- 2012-0047 - Response to Horizon Utility Corporation (HUC) letter dated April 10, 2014

When the Board orders the transfer of customers between utilities, Hydro One believes that the fundamental test of valuation must be the "no-harm" test. Like the customers of all LDCs, Hydro One customers with generally similar characteristics are included in a series of rate pools. The customers in Parts II & III of this SAA have a lower than average cost of service since they have a higher than average asset density compared to other customers in their pool. However, all the customers in the pool pay the same rate. Therefore, the average margin is higher than average for these customers. The present value of the future margin is higher than the NBV of the assets required to serve these customers. If the purchase price that is ultimately paid is NBV ($44k) then the credit to the pool will be less than the Present Value of the future margin of these customers ($156 k) that would have ultimately accrued to the benefit of the pool. In that event then the pool will suffer a deficit for which the only remedy is higher rates to the remaining customers.

Attached as Appendix A to this letter are the details of the calculations which formulate the estimated customer value of approximately $156k. Appendix B attached includes the detailed asset schedule for the specific customers which sums to approximately $44k. These items, along with significant supporting information, were previously provided to HUC at face-to-face meetings held on a number of occasions in 2013.

Understanding that there was a significant difference in the value presented, Hydro One had been attempting to work cooperatively with HUC on a resolution. At the meeting in October, the parties had agreed to collaboratively request guidance from the Board to reach a fair compromise. The process that was agreed to was that the two parties would submit a joint letter to the Board asking for direction to assist in resolution. Hydro One committed to writing a first draft of that letter, a copy of which was sent to HUC on November 1, 2013. The email, including the draft letter, is attached as Appendix C. Hydro One followed up on the draft but did not receive a response.

Notwithstanding the harm that will invariably come to the rate pools described above should the purchase be executed at NBV, Hydro One also recognizes that these pools contain billions of dollars of assets and the amount in question in this matter is a few thousand dollars. Hydro One has been seeking a reasonable, negotiated settlement to close this matter once and for all. However, Hydro One notes that any decision or action taken here should not serve as a precedent for a larger population of customers in a similar situation.

Hydro One stands ready to provide any information that the Board might find helpful in determining the outcome of this matter.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank
VP & Chief Regulatory Officer

attachments

Estimated Customer Value

Valuation Summary

	Residential	Commercial	Total
Total Estimated Margin (all customers)	3,318	16,912	20,230
Income Tax on Margin	(879)	(4,482)	(5,361)
Average Annual Capital Expenditures	(410)	(2,090)	(2,500)
Estimated Free Cash Flow	2,029	10,341	12,369
Net Present Value of Free Cash Flow	25,608	130,525	**156,133**

Assumptions

Income Tax Rate	26.5	%
WACC	6.1	%
Study Period	25	years

Annual Average	Customers *	Load (kWh) #	Dist. Revenue	OM&A ^
Residential	10	83,185	4,990	1,672
Commercial	3	950,566	22,104	5,192

Capital Expenditures ^ Estimated $100,000 over 40 years = $2,500 per year

* Not all units were occupied at all times
Numbers are actual revenues receveied no averaging is done for smaller customer numbers
\# Based on a 15 month sampling of data from January 2012 to March 2013
^ Estimates based on customer averages within the relevant rate class given that sample size is too small
Using observed actuals for these 13 customers leads to a higher overall valuation (approx. $193k)

Asset	Capitalized Date	Asset description	Acquis.val.	Accum.dep.	Book val.	Currency	Qty	Qty/% requested	Cost	NBV
180000001454	1965.07.05	DX-RURAL OH TRFRMRS <=25 KVA	68,259	(66,757)	1,502	CAD	400	1	171	4
180000002022	1970.07.05	DX-RURL OH TRFMRS >25&<=50 KVA	18,170	(15,986)	2,184	CAD	51	1	356	43
180000008238	1971.07.05	DX-RURAL CONDUCTOR	170,079	(168,513)	1,567	CAD	246,456	286	197	2
180000008238	1971.07.05	DX-RURAL CONDUCTOR	170,079	(168,513)	1,567	CAD	246,456	94	65	1
180000003006	1971.07.05	DX-INSTALL RURAL TRANSFORMERS	3,069	(2,495)	574	CAD	17	1	181	34
180000003006	1971.07.05	DX-INSTALL RURAL TRANSFORMERS	3,069	(2,495)	574	CAD	17	1	181	34
180000031758	1992.07.05	DX-RURL OH TRFMRS>50&<=75 KVA	9,204	(4,337)	4,868	CAD	5	3	5,523	2,921
180000032945	1993.07.05	DX-INSTALL RURAL TRANSFORMERS	103,345	(44,983)	58,363	CAD	95	3	3,264	1,843
180000034040	1994.07.05	DX-RURAL OH TRFRMRS <=25 KVA	133,213	(56,617)	76,596	CAD	130	1	1,025	589
180000034034	1994.07.05	DX-INSTALL RURAL TRANSFORMERS	201,962	(85,836)	116,126	CAD	211	1	957	550
180000035114	1995.07.05	DX-RURL OH TRFMRS >25&<=50 KVA	45,144	(18,146)	26,998	CAD	36	2	2,508	1,500
180000035105	1995.07.05	DX-INSTALL RURAL TRANSFORMERS	71,183	(28,612)	42,570	CAD	73	2	1,950	1,166
180000075196	1999.07.05	DX - U/GRD CONDTR SEC SERV	348,945	(161,730)	187,215	CAD	7,119	91	4,460	2,393
180000041794	2001.01.31	DX-RURAL OH TRFRMRS <=25 KVA	221,102	(57,840)	163,262	CAD	234	3	2,835	2,093
180000041790	2001.01.31	DX-INSTALL RURAL TRANSFORMERS	153,234	(39,700)	113,534	CAD	130	3	3,536	2,620
180000098071	2010.01.29	RURAL OH TRFRMRS <=25 KVA	15,683	(888)	14,795	CAD	12	1	1,307	1,233
180000098070	2010.01.29	RURAL OH TRFMRS >25&<=50 KVA	30,989	(1,298)	29,690	CAD	7	1	4,427	4,241
180000098068	2010.01.29	RURAL TRSF INSTAL	134,824	(6,599)	128,225	CAD	20	2	13,482	12,823
180000102543	2011.02.24	RURAL OH TRFRMRS <=25 KVA	2,623	(111)	2,512	CAD	2	1	1,311	1,256
180000102544	2011.02.24	RURAL CONDUCTOR PRIM&SEC OVERH	8,485	(318)	8,167	CAD	215	75	2,960	2,849
180000102542	2011.02.24	RURAL TRSF INSTAL	12,285	(449)	11,837	CAD	2	1	6,143	5,918
180000104745	2012.01.31	RURAL CONDUCTOR PRIM&SEC OVERH	219,582	(3,524)	216,057	CAD	46,804	70	328	323
								Total	**57,166**	**44,435**

From: FRANK Susan
Sent: Friday, November 01, 2013 5:21 PM
To: Indy J. Butany-DeSouza (indy.butany@horizonutilities.com)
Subject: Draft - HONI/HUC letter to OEB on customer value

At our last meeting I had indicated that we would draft a letter to the OEB seeking guidance on the appropriate value to transfer the 13 customers. Please find attached my proposal. Let me know if this is acceptable to Horizon.

Susan

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Susan Frank
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BY COURIER

November 1, 2013

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

Dear Ms. Walli:

EB-2012-0047 – Horizon Utilities Corporation – Application for Service Area Amendment – Request for Direction on Valuation of Existing Customers

I am writing to you on behalf of Hydro One Networks and Horizon Utilities Corporation.

In the above noted proceeding, the Board was asked to determine whether the service area of Horizon Utilities Corporation ("HUC") should be amended to include certain territories currently in the licence area of Hydro One Networks Inc. ("HONI"). The territories described in the application were divided into five different parts. This Service Area Amendment ("SAA") was somewhat unique insofar as it involved the transfer of existing customers ("the affected customers") currently served by HONI. Parts II & III were comprised of approximately 13 existing commercial and residential customers bounded in whole or in part by the existing territories of HUC. In the Board's decision issued on March 15, 2013, the Board granted both of these parts of the application and thereby determined that the affected customers should be served by HUC going forward.

What was not set out in the March 15 decision of the Board was the value that should be attributed to the affected customers. HUC and HONI have participated in discussions with respect to the transfer of the relevant parts of the SAA as prescribed in the March 15th decision. The parties can report that these discussions have been productive and we look forward to resolution on a number of items. All parties agree that some payment should be made by HUC to HONI as consideration for the transfer of the affected customers. However, specific precedent from a SAA proceeding that would provide guidance as to the amount of the payment does not appear to be available. As a result, the parties have jointly agreed to seek, by way of this letter, the Board's guidance in determining the value that should be paid for the affected customers.

There are two options that have been discussed by the parties.

1. Net Book Value of the Assets.
    - Hydro One has comprised a detailed listing of the assets that are currently used to serve the existing customers. A snapshot of this listing is included as Attachment 1. This type of value would be typically found between utilities in a Long-Term Load Transfer (LTLT) arrangement.
    - The concept is that the cost of installing these assets was prudently incurred in order to provide service to these customers. The depreciated value of the assets currently resides in the Rate Base of HONI. The expectation would be that the value of these assets would be allowed into the Rate Base of HUC and they would be allowed to recoup a normal regulatory return on that value.
    - The proposed payment under this option is $44,447

2. Present Value of the Future Margin
    - HONI has estimated the average margin that it currently receives from the customers to be transferred as a result of the SAA. Furthermore, the present value of the future margin that would have reasonably been expected to be collected by HONI has been calculated. A summary of those calculations has been included as Attachment 2. This methodology is most common during a sale of a group of customers from one utility to another.
    - HONI rates are designed based on a provincial population of customers. Those customers that reside in more dense regions close to other dense service territories often garner a margin that is higher than average. Removing that margin from the rate class has a disproportionate effect on the other remaining rate payers of HONI. As a result, the other HONI customers must, all things being equal, provide more revenue to fund the activities of the utility. It is typical that these types of customer sales are done at a premium to the book value of the assets.
    - It is expected that the value paid for the affected customers by HUC under this option would be allowed in the Rate Base of HUC and that they would be allowed to recoup a normal regulatory return on that value.
    - The proposed payment under this option is $156,133.

HONI and HUC respectfully request that the Board review and determine, by whatever means it deems necessary, which of the above methods is appropriate in valuing the affected customers. If it is helpful to the panel, the parties are prepared to provide further submissions of detail regarding the matter. However, neither party is desirous of incurring the cost and time associated with a full proceeding.

We make this request on a joint basis in the spirit of resolution. We trust this is satisfactory.

An electronic copy of the Interrogatories, have been filed using the Board's Regulatory Electronic Submission System.

Sincerely,

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK AND INDY BUTANY-DESOUZA

Susan Frank
Vice President and Chief Regulatory Officer
Hydro One Networks Inc.

Indy J. Butany-DeSouza
Vice President, Regulatory Affairs
Horizon Utilities Corporation

Attachment 1

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^ Based on customer averages within the R1 rate class