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Cost of Capital and Rate of Return

Ex.5/Tab 1/Sch.1 - Capital Structure

WNP seeks to recover a weighted average cost of capital of 5.99% through rates in the 2016 Test Year. WNP has followed the Report of the Board on Cost of Capital for Ontario's Regulated Utilities, December 11, 2009 in determining the cost of capital.

In calculating the cost of capital, WNP has used the OEB's deemed capital structure of 56% long-term debt, 4% short-term debt, and 40% equity as the Cost of Capital parameters in the OEB's letter of October 15, 2015 for the allowed return on equity ("ROE").

WNP's cost of capital for 2016 has been calculated as 5.99%, as shown in the table below:

Table 5.1: Overview of Capital Structure

Particulars	Cost Rate
	(%)
Debt	
Long-term Debt	4.01
Short-term Debt	1.65
Total Debt	4.35
Equity	
Common Equity	9.19
Preferred Shares	0.00
Total Equity	9.19
Total	5.99

The Cost of Capital parameters are consistent with the letter issued by the OEB on October 15, 2015 that sets the values as indicated below:

Table 5.2: 2016 Rate Applications – Capital Parameters

Cost of Capital Parameter	Value for 2016 Applications for Rate Changes in 2016
Return on Equity (ROE)	9.19%
Deemed Long-Term Debt rate	4.54%
Deemed Short-Term Debt rate	1.65%

WNP understands that the OEB may update the ROE for 2016 at a later date, and therefore the LDCS commits to updating its Application to reflect the OEB's updated Cost of Capital Parameters for May 1, 2016 applications and as new information is issued.

Ex.5/Tab 1/Sch.2 - OEB Appendix 2-OA Capital Structure / Cost of Capital

Appendix 2-OA below presents the capital structure for the last Board Approved (2012) and the 2016 Test year.

Table 5.3: 2012, 2016 Capital Structure

Board Appr. Year: 2012					
Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$4,194,018	4.42%	\$185,376
2	Short-term Debt	4.00% (1)	\$299,573	2.08%	\$6,231
3	Total Debt	60.0%	\$4,493,591	4.26%	\$191,607
	Equity				
4	Common Equity	40.00%	\$2,995,727	9.12%	\$273,210
5	Preferred Shares	0.00%	\$ -	0.00%	\$ -
6	Total Equity	40.0%	\$2,995,727	9.12%	\$273,210
7	Total	100.0%	\$7,489,318	6.21%	\$464,817

Year: 2016					
Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$5,331,409	4.01%	\$213,789
2	Short-term Debt	4.00% (1)	\$380,815	1.65%	\$6,283
3	Total Debt	60.0%	\$5,712,224	3.85%	\$220,073
	Equity				
4	Common Equity	40.00%	\$3,808,149	9.19%	\$349,969
5	Preferred Shares		\$ -		\$ -
6	Total Equity	40.0%	\$3,808,149	9.19%	\$349,969
7	Total	100.0%	\$9,520,373	5.99%	\$570,042

Ex.5/Tab 1/Sch.3 - OEB Appendix 2-OB Cost of Debt Instruments

Appendix 2-OB below presents capital structure for all required historical years, the 2015 Bridge Year and the 2016 Test year, illustrating the weighted average cost of long-term debt.

Table 5.4: 2012 to 2016 Debt Instruments

Debt Instruments										
Year 2016										
Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable- Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	Promissory Note	Township of Wellington North	Third-Party	Fixed Rate	1/Nov/01		\$ 985,016	4.54%	\$ 44,719.73	
2	Smart Meter Funding	Infrastructure Ontario	Third-Party	Fixed Rate	1/Jun/11	15	\$ 913,371	4.42%	\$ 40,371.00	
3	Capital Projects (2008 & 2009)- Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	5	\$ 318,627	2.46%	\$ 7,838.21	
4	Capital Projects (2008 & 2009)- Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	30	\$ 1,074,216	4.49%	\$ 48,232.30	
5	MS2 Substation Re-Build (2014)	Infrastructure Ontario	Third-Party	Fixed Rate	2/Apr/15	30	\$ 1,132,889	3.28%	\$ 37,158.77	
6	Secondary Feed Loan	Infrastructure Ontario	Third-Party	Fixed Rate	2/Jul/16	30	\$ 1,200,000	3.95%	\$ 47,400.00	Rate Based on IO rate on Oct 15, 2015
Total							\$ 5,624,119	4.01%	\$ 225,720.01	
Year 2015										
Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable- Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	Promissory Note	Township of Wellington N	Third-Party	Fixed Rate	1/Nov/01		\$ 985,016	4.41%	\$ 43,439.21	
2	Smart Meter Funding	Infrastructure Ontario	Third-Party	Fixed Rate	1/Jun/11	15	\$ 980,943	4.42%	\$ 43,357.66	
3	Capital Projects (2008 & 2009) - Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	5	\$ 422,717	2.46%	\$ 10,398.85	
4	Capital Projects (2008 & 2009) - Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	30	\$ 1,093,091	4.49%	\$ 49,079.80	
5	MS2 Substation Re-Build (2014)	Infrastructure Ontario	Third-Party	Fixed Rate	2/Apr/15	30	\$ 1,150,000	3.28%	\$ 28,290.00	Nine months in 2015
Total							\$ 4,631,767	3.77%	\$ 174,565.51	
Year 2014										
Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable- Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	Promissory Note	Township of Wellington N	Third-Party	Fixed Rate	1/Nov/01		\$ 985,016	4.41%	\$ 43,439.21	
2	Smart Meter Funding	Infrastructure Ontario	Third-Party	Fixed Rate	1/Jun/11	15	\$ 1,045,598	4.42%	\$ 46,215.42	
3	Capital Projects (2008 & 2009)- Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	5	\$ 524,281	2.46%	\$ 12,897.32	
4	Capital Projects (2008 & 2009)- Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	30	\$ 1,111,139	4.49%	\$ 49,890.15	
Total							\$ 3,666,034	4.16%	\$ 152,442.10	
Year 2013										
Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable- Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	Promissory Note	Township of Wellington N	Third-Party	Fixed Rate	1/Nov/01		\$ 985,016	4.41%	\$ 43,439.21	
2	Smart Meter Funding	Infrastructure Ontario	Third-Party	Fixed Rate	1/Jun/11	15	\$ 1,107,462	4.42%	\$ 48,949.83	
3	Capital Projects (2008 & 2009) - Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	5	\$ 532,633	2.46%	\$ 1,091.90	One month in 2013
4	Capital Projects (2008 & 2009) - Re-Financing	Infrastructure Ontario	Third-Party	Fixed Rate	2/Dec/13	30	\$ 1,112,607	4.49%	\$ 4,163.00	One month in 2013
Total							\$ 3,737,718	2.61%	\$ 97,643.94	
Year 2012										
Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable- Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) (Note 2)	Interest (\$) (Note 1)	Additional Comments, if any
1	Promissory Note	Township of Wellington N	Third-Party	Fixed Rate	1/Nov/01		\$ 985,016	4.41%	\$ 43,439.21	
2	Smart Meter Funding	Infrastructure Ontario	Third-Party	Fixed Rate	1/Jun/11	15	\$ 1,166,657	4.42%	\$ 51,566.23	
Total							\$ 2,151,673	4.42%	\$ 95,005.44	

1 In 2016, WNP is planning a major capital project - the construction of a 2nd 44kV Feeder with an
2 estimated cost of approximately \$1,200,000 which the LDC will finance through a long-term loan
3 with Infrastructure Ontario.

4 In filing this rate application, WNP has also filed its Distribution System Plan (in Exhibit 2,
5 Appendix 2A) which, in section 5.4.5.3. – “Special Projects” includes the details concerning the
6 Second 44kV Feeder to Mount Forest. Currently, there is only one feeder to this area which is
7 at its demand capacity and has been affected by reliability in recent years. This project is in
8 conjunction with Hydro One.) WNP (WNP) has been working with Hydro One Networks Inc.
9 (HONI) to address capacity and reliability concerns with the electrical supply to Mount Forest.
10 The result is a proposed project, pending OEB approval, to build approximately 11 kilometers of
11 pole line to connect a 44kV feeder from Palmerston TS to WNP’s distribution system.

12 Mount Forest is supplied through a single rural radial 44kV pole line owned and operated by
13 HONI from the Hanover TS approximately 44km away. The existing pole line is constructed
14 through several areas with no road access making inspection, maintenance and repairs difficult
15 and time consuming. An ice storm in April 2013 broke a number of HONI poles resulting in an
16 outage lasting over 18 hours negatively impacting the manufacturing and small business
17 consumers as well as critical load customers in Mount Forest. The outage demonstrated the
18 need for an alternate power supply to ensure critical loads (hospital, seniors housing complex
19 and warming station) are maintained and switching options are available to transfer loads.

20 As discussed in WNP’s Distribution System Plan, the Applicant is seeking Board approval to
21 build a 2nd feeder line to one of its service territories (the Town of Mount Forest) and recover
22 the construction costs through the utility’s distribution rates, commencing May 1, 2016.

23 WNP has spoken with Infrastructure Ontario regarding financing this project. Infrastructure
24 Ontario (IO) conducted a preliminary review using WNP’s latest Financial Audit Statement
25 (2014) and advised that:

26 “Based on a preliminary review of the project details and Wellington North’s 2014 Financial
27 Statements Wellington North Power would be within IO’s current Debt Service Coverage Ratio
28 and Debt to Total Assets Ratio requirements after financing \$1,201,640 for this project.”

WNP would be applying for a loan application with a 30-year amortization period, which attracts an interest rate of 3.95% (based on published rates as at October 15th 2015).

To date, WNP has incurred the following expenses in relation to this project:

- a) Commissioned Hydro One to perform a capacity study of the current feeder line to Mount Forest at a cost of \$32,061. This study is included in Appendix D of WNP's Distribution System Plan and describes the options that have been reviewed;
- b) A Purchase Order for \$61,668 to Hydro One to for easement activity in relation to the route the proposed 2nd feeder would run.

In WNP's Distribution System Plan, Appendix D – "Hydro One: Town of Mount Forest Supply Study"), page 17 indicates that for the preferred option, total cost (based on 2013 costs) is \$2,403,280, of which WNP would responsible for 50% of the cost of the work, or \$1,201,640. WNP anticipate this cost will be a capital contribution payment to Hydro One. Hydro One has explored several options and believes the most effective and cost-efficient solution will be to extend the Palmerston TS M2 feeder up to WNP's service boundary.

Should WNP receive OEB approval to recover construction costs of this project through the LDC's distribution electricity rates effective from May 1, 2016, the above incurred costs will be capitalized as a capital investment project.

Ex.5/Tab 1/Sch.4 - Cost of Capital

This evidence summarizes the capital structure, method and cost of financing WNP's capital requirements for the 2016 Test Year.

Capital Structure

The estimated cost rates for cost of capital in 2016 are presented on the first page of Exhibit 5 / Tab 1 / Schedule 2. The rates shown for short-term debt and return on equity are those set out in the Board's letter October 16, 2015, "Cost of Capital Parameter Updates for 2016 Cost of Service Applications".

WNP proposes a Long Term Debt cost rate for 2016 of 4.01% as calculated in Appendix 2-OB for 2016 as displayed in Table 5.4 above.

WNP's current OEB-approved capital structure for rate-making purposes is 60% debt and 40% equity. WNP intends to maintain the same capital structure in the 2016 Test Year. This capital structure was confirmed by the OEB in the Report of the Board on Cost of Capital for Ontario's Regulated Utilities dated December 11, 2009 (The "Board Report"). The 60% debt component is comprised of 4.0% deemed short-term debt and 56.0% deemed long-term debt.

Return on Equity

WNP has used a ROE of 9.19% in 2016 as established by the Board for cost of service applications with 2016 implementation date.

Weighted Average Cost of Debt

WNP proposes a Long Term Debt cost rate for 2016 of 4.01% which is below the OEB's Deemed Long-Term debt rate of 4.54 as prescribed in the Board's letter of October 15, 2015 "Cost of Capital Parameter Updates for 2016 Cost of Service Applications".

Long Term Debt

WNP's Long Term Debt instruments (both existing and proposed) are summarized below. For a numerical presentation please refer to Exhibit 5 / Tab 1 / Schedule 3.

- Promissory Note – The remaining amount of \$985,016 is has an interest rate that matches the Cost of Capital parameters issued by the OEB. The current interest rate of 4.41% will be increasing to the new rate of 4.54% upon approval of this application. This debt is held by the majority shareholder, the Township of Wellington North and no principal is currently being paid. The full Promissory Note to Wellington North Power Inc. secondary shareholder, Township Southgate, in the amount of \$49,388 has been repaid.
- Ontario Infrastructure and Lands Corporation Convertible Loan – WNP borrowed \$1,200,000 in 2011 to fund smart meter investments. The loan was for a 15 year period with interest at 4.42%. Repayment of the fixed rate long-term loan is made through blended (i.e., principal and interest) monthly payments of \$9,130.93. The outstanding principal amount for 2016 is \$913,371 as displayed in table 5.4 above.
- Ontario Infrastructure and Lands Corporation Convertible Loan - WNP borrowed \$532,633 in 2013 to fund capital projects that had previously been completed. The loan was for a 5 year period with interest at 2.46%. Repayment of the fixed rate long-term loan is made through blended (i.e., principal and interest) monthly payments of

\$9,443.44. The outstanding principal amount for 2016 is \$318,627 as displayed in table 5.4 above.

- Ontario Infrastructure and Lands Corporation Convertible Loan - WNP borrowed \$1,112,607 in 2013 to fund capital projects that had previously been completed. The loan was for a 30 year period with interest at 4.49%. Repayment of the fixed rate long-term loan is made through blended (i.e., principal and interest) monthly payments of \$5,630.81. The outstanding principal amount for 2016 is \$1,074,216 as displayed in table 5.4 above.

- Ontario Infrastructure and Lands Corporation Convertible Loan - WNP borrowed \$1,150,000 in 2015 to fund the MS-2 Sub-station rebuild that was completed in 2014. The loan was for a 30 year period with interest at 3.28%. Repayment of the fixed rate long-term loan is made through blended (i.e., principal and interest) monthly payments of \$5,023.83. The outstanding principal amount for 2016 is \$1,132,889 as displayed in table 5.4 above.

- Ontario Infrastructure and Lands Corporation Convertible Loan – In the 2016 Test Year WNP is projecting a loan of \$1,200,000 to fund the proposed capital contribution payable to Hydro One Networks Inc. for a second line feeder to Mount Forest. Current Infrastructure Ontario rates are 3.95% which would result in a blended monthly payment of \$5,694.45. Interest rates have been steadily increasing in 2015.

Short Term Debt

WNP has used a short-term debt rate of 1.65% for 2016 as established by the Board for cost of service applications with an April 30, 2016 implementation date.

WNP's Short Term Debt instruments are summarized below.

- Revolving Line of Credit: In 2014, WNP had access to a revolving line of credit facility in the amount of \$1,000,000 that is secured by a general security agreement over the Corporation's assets. WNP required a temporary bulge loan to finance the MS-2 Sub-station rebuild due to delays in the processing of the Infrastructure Ontario loan

1 application submitted in Aug 2014. In June of 2015 the line of credit amount was
2 increased to \$1,500,000.

- 3 • Letter of Credit: WNP has obtained a Letter of Credit from a Canadian bank in the
4 amount of \$558,879 that has been issued in favour of the Independent Electricity
5 System Operator (IESO). This Letter of Credit financially secures the Corporation's
6 electricity purchases from the IESO, who has not drawn on this credit instrument.

7 WNP is aware that the IESO is reviewing its prudential requirements and undertakes to update
8 this evidence at a later date for any changes in these requirements authorized by the IESO.

9 WNP does not forecast that it will redeem any debt and has not issued any preference shares,
10 hence WNP does not record either a profit or a loss on redemption of debt and/or preference
11 shares.

12 OEB Appendix 2-OB Cost of Debt Instruments in Exhibit 5 / Tab 1 /Schedule 3 detailed WNP's
13 long-term debt.

14 **Notional Debt**

15 Notional debt is the portion of deemed debt that results from differences between the WNP's
16 actual debt and the deemed debt of 60% of the rate base. With the planned loan in 2016,
17 WNP's actual long-term debt will be within 2% of the 60% deemed debt. It is anticipated that
18 WNP's Notional debt will continue to be low since as the rate base grows and debt is repaid,
19 additional loans will be required to finance future capital projects.

20 **Not-For-Profit**

21 Note that WNP is not a cooperative and as such, all requirements related to a not-for-profit
22 organization do not apply.

Appendix

List of Appendices

Appendix 5A	Promissory Note to the Township of Wellington North.

Appendix 5A – Promissory Note

Promissory Note with Township of Wellington North:

PROMISSORY NOTE

Principal Sum: **\$1,585,016.00**

FOR VALUE RECEIVED, the undersigned hereby unconditionally promises to pay to the order of the Corporation of the Township of Wellington North (the “**Township**”) on demand by the Township the principal sum of **\$1,585,016.00 DOLLARS** (the “**Principal Sum**”) in lawful money of Canada at [7490 Sideroad 7 West], Kenilworth, Ontario or such other place as the Township may designate by notice in writing to the undersigned and to pay interest on the Principal Sum at the rate of 7.25 % per annum calculated and accruing on the principal amount remaining unpaid and overdue interest, if any from [November 1, 2001] until the Principal Sum is repaid to the Township. Interest shall be calculated and payable quarterly in arrears on [the last day of March, June, September and December] at the same address with the first interest payment payable on [March 31, 2002]. Interest both before and after default and judgment on the principal amount and overdue interest shall be payable at the aforementioned rate. For greater certainty, no interest shall accrue or be payable by the undersigned to the Township on the Principal Sum for the date hereof to [November 1, 2001].

All payments or any part thereof may be extended, rearranged, renewed or postponed by the Township. No delay or failure by the Township to exercise any right or remedy against the undersigned shall be construed as a waiver of that or any right or remedy nor shall any waiver hereunder be deemed to be a waiver of subsequent default. The Township may, at any time, in accordance with the provisions of Township By-Law 32-2000, as amended, by By-Law 51-00 and By-Law 54-2000 and after consultation with the undersigned, replace this promissory note for one or more debt instruments of the undersigned with any change to any provision hereunder, including reducing or increasing the rate of interest payable on the principal amount owing at the time of replacement, setting a date on which the principal amount hereunder is due and payable or adjusting the principal sum payable hereunder, all as evidenced by the written acceptance by said debt instrument or instruments by the Treasurer of the Township.

The undersigned hereby waives presentment, demand, protest or other notice of every kind in the enforcement of this promissory note. All amounts owing hereunder will be paid by the undersigned without regard for any equities between the undersigned and the Township or any right of set-off or cross-claim.

In the event of a default hereunder, the undersigned agrees to pay all expenses, including without limitation, reasonable legal fees (on a solicitor and his own client basis), incurred by the Township in endeavoring to enforce its rights hereunder. All such amounts shall bear interest at the rate mentioned above.

This promissory note is non-negotiable and non-assignable without prior written consent of the undersigned.

DATE at Mount Forest, Ontario, as of the 1st day of July, 2000.

WELLINGTON NORTH POWER INC.

By: _____

Chairman

By: _____

Secretary