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Cost of Capital and Rate of Return

Ex.5/Tab 1/Sch.1 – Overview

Rideau St. Lawrence Distribution Inc. (“RSL”) seeks to recover a weighted average cost of capital of 5.62% through rates in the 2016 Test Year. RSL 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, RSL has used the OEB’s deemed capital structure of 56% for long-term debt, 4% for short-term debt, and 40% for equity, and the Cost of Capital parameters in the OEB’s letter of October 15, 2015, for the allowed return on equity (“ROE”). RSL recognizes that the Cost of Capital parameters will be updated in accordance with Board guidelines and as such commits to updating the cost capital parameters as new information is made available.

RSL’s cost of capital for 2016 has been calculated as 5.62%, as shown in the table below:

Table 5.1: Cost of Capital

Particulars	Cost Rate
	(%)
Debt	
Long-term Debt	3.36%
Short-term Debt	1.65%
Total Debt	3.25%
Equity	
Common Equity	9.19%
Preferred Shares	0
Total Equity	9.19%
Total	5.62%

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

Table 5.2: 2016 Rate Applications – Capital Parameters

Cost Capital Parameter	Value for 2016 Application 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%			

Ex.5/Tab 1/Sch.2 – Appendix 2-OA & 2-OB

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

Table 5.3: Appendix 2-OA – Cost of Capital & Debt Structure

Appendix 2-OA					
Capital Structure and Cost of Capital					
This table must be completed for the last Board approved year and the test year.					
Year: 2016 Test Year					
Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$3,942,795	3.36%	\$132,478
2	Short-term Debt	4.00% (1)	\$281,628	1.65%	\$4,647
3	Total Debt	60.0%	\$4,224,423	3.25%	\$137,125
	Equity				
4	Common Equity	40.00%	\$2,816,282	9.19%	\$258,816
5	Preferred Shares		\$ -		\$ -
6	Total Equity	40.0%	\$2,816,282	9.19%	\$258,816
7	Total	100.0%	\$7,040,705	5.62%	\$395,941
Notes					
(1)	4.0% unless an applicant has proposed or been approved for a different amount.				
This table must be completed for the last Board approved year and the test year.					
Year: 2012 Board Approved					
Line No.	Particulars	Capitalization Ratio		Cost Rate	Return
		(%)	(\$)	(%)	(\$)
	Debt				
1	Long-term Debt	56.00%	\$3,971,768	3.75%	\$148,941
2	Short-term Debt	4.00% (1)	\$283,698	2.08%	\$5,901
3	Total Debt	60.0%	\$4,255,466	3.64%	\$154,842
	Equity				
4	Common Equity	40.00%	\$2,836,977	9.12%	\$258,732
5	Preferred Shares		\$ -		\$ -
6	Total Equity	40.0%	\$2,836,977	9.12%	\$258,732
7	Total	100.0%	\$7,092,444	5.83%	\$413,575

Appendix 2-OB below presents debt instruments for all required historical years and the Test year.

Table 5.4: Appendix 2-OB – Debt Instruments

Year

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) ²	Interest (\$) ¹	Additional Comments, if any
1	Altec Line Truck	Bank of Montreal	Third-Party	Variable Rate	1-Dec-09	10	\$ 183,750	2.77%	\$ 5,087.01	
2	Posi Plus	Bank of Montreal	Third-Party	Fixed Rate	1-Sep-11	8	\$ 273,727	3.57%	\$ 9,780.07	
3	Smart Meters	Bank of Montreal	Third-Party	Variable Rate	1-Jul-10	10	\$ 922,289	2.84%	\$ 26,186.59	
4	Promissory Note	Township of Edwardsburgh/Cardinal	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 225,000	4.70%	\$ 10,575.02	
5	Promissory Note	Township of South Dundas	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 938,352	4.70%	\$ 44,102.54	
Total							\$ 2,543,118	3.76%	\$ 95,731.23	

Year

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) ²	Interest (\$) ¹	Additional Comments, if any
1	Altec Line Truck	Bank of Montreal	Third-Party	Variable Rate	1-Dec-09	10	\$ 153,125	2.72%	\$ 4,166.70	
2	Posi Plus	Bank of Montreal	Third-Party	Fixed Rate	1-Sep-11	8	\$ 238,407	3.54%	\$ 8,435.59	
3	Smart Meters	Bank of Montreal	Third-Party	Variable Rate	1-Jul-10	10	\$ 815,614	2.82%	\$ 22,980.85	
4	Promissory Note	Township of Edwardsburgh/Cardinal	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 225,000	4.41%	\$ 9,922.51	
5	Promissory Note	Township of South Dundas	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 938,352	4.41%	\$ 41,381.32	
Total							\$ 2,370,499	3.67%	\$ 86,886.97	

Year

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) ²	Interest (\$) ¹	Additional Comments, if any
1	Altec Line Truck	Bank of Montreal	Third-Party	Variable Rate	1-Dec-09	10	\$ 122,500	2.65%	\$ 3,248.35	
2	Posi Plus	Bank of Montreal	Third-Party	Fixed Rate	1-Sep-11	8	\$ 203,088	3.49%	\$ 7,094.09	
3	Smart Meters	Bank of Montreal	Third-Party	Variable Rate	1-Jul-10	10	\$ 708,940	2.79%	\$ 19,782.08	
4	Promissory Note	Township of Edwardsburgh/Cardinal	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 225,000	4.41%	\$ 9,922.50	
5	Promissory Note	Township of South Dundas	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 938,352	4.41%	\$ 41,381.32	
Total							\$ 2,197,880	3.70%	\$ 81,428.34	

Year

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) ²	Interest (\$) ¹	Additional Comments, if any
1	Altec Line Truck	Bank of Montreal	Third-Party	Variable Rate	1-Dec-09	10	\$ 91,875	2.65%	\$ 2,436.26	
2	Posi Plus	Bank of Montreal	Third-Party	Fixed Rate	1-Sep-11	8	\$ 167,768	3.49%	\$ 5,860.34	
3	Smart Meters	Bank of Montreal	Third-Party	Variable Rate	1-Jul-10	10	\$ 602,265	2.79%	\$ 16,805.46	
4	Promissory Note	Township of Edwardsburgh/Cardinal	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 225,000	4.41%	\$ 9,922.50	
5	Promissory Note	Township of South Dundas	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 938,352	4.41%	\$ 41,381.32	
Total							\$ 2,025,261	3.77%	\$ 76,405.88	

Notes

Year

Row	Description	Lender	Affiliated or Third-Party Debt?	Fixed or Variable-Rate?	Start Date	Term (years)	Principal (\$)	Rate (%) ²	Interest (\$) ¹	Additional Comments, if any
1	Altec Line Truck	Bank of Montreal	Third-Party	Variable Rate	1-Dec-09	10	\$ 61,250	2.65%	\$ 1,624.18	
2	Posi Plus	Bank of Montreal	Third-Party	Fixed Rate	1-Sep-11	8	\$ 132,449	3.49%	\$ 4,626.58	
3	Smart Meters	Bank of Montreal	Third-Party	Variable Rate	1-Jul-10	10	\$ 495,591	2.79%	\$ 13,828.84	
4	Promissory Note	Township of Edwardsburgh/Cardinal	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 225,000	4.41%	\$ 9,922.50	
5	Promissory Note	Township of South Dundas	Affiliated	Fixed Rate	1-Aug-01	Demand	\$ 938,352	4.41%	\$ 41,381.32	
6	Posi Digger Truck	Bank of Montreal	Third-Party	Variable Rate	6-May-16	10	\$ 114,000	2.70%	\$ 2,052.00	
7	Posi Digger Truck	Bank of Montreal	Third-Party	Variable Rate	1-Oct-16	10	\$ 276,000	2.70%	\$ 1,863.00	
Total							\$ 2,242,642	3.36%	\$ 75,298.43	

Ex.5/Tab 1/Sch.3 – Rates of Capital Cost

The proposed rates for cost of capital in 2016 are presented in Table 5.3 of Ex.5/Tab.1/Sch.2. The rates shown for short-term debt and return on equity are those set out in the Board's letter of October 15, 2016, "Cost of Capital Parameter Updates for 2016 Cost of Service Applications".

RSL proposes a Long Term Debt cost rate for 2016 of 3.36% as calculated in Appendix 2-OB for 2016 as displayed in Table 5.4 above.

RSL's current OEB-approved capital structure for rate-making purposes is 60% debt and 40% equity. RSL 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

RSL has used a ROE of 9.19% in 2016 as established by the Board for cost of service applications with a May 1, 2016 implementation date. RSL recognizes that the ROE may be updated in accordance with Board guidelines and as such commits to updating the cost capital parameters as new information is made available.

Long Term Debt

RSL proposes a Long Term Debt cost rate for 2016 of 3.36% 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".

RSL's Long Term Debt instruments are summarized below.

- Promissory Note – RSL has two promissory notes with its shareholders, \$225,000 with the Township of Edwardsburgh/Cardinal, \$998,352 with the Township of South Dundas. The note for South Dundas was issued on October 31, 2000 with term on demand. The note for Edwardsburgh/Cardinal was issued on July 15, 2001 with term on demand. The notes have an interest rate that is determined by the Directors of RSL, and is not to exceed an annual rate of 7.25%. The current interest rate is set at 4.41%, based on Cost of Capital Parameters as of May 1, 2012.
- Bank debt – RSL has planned a major capital purchase in 2016 - the purchase of a Posi Digger Truck with a cost of approximately \$390,000. The LDC will finance the purchase through two long-term loans with the Bank of Montreal. RSL also has three bank loans with the Bank of Montreal issued in 2009, 2010 and 2011 respectively. The details of the Long-Term Bank Debt with BMO are reflected in Table 5.4 above.

Short Term Debt

RSL has used a short-term debt rate of 1.65% for the 2016 test year as established by the Board for cost of service applications with a May 1, 2016 implementation date. RSL recognizes that the short-term debt rate may be updated at a later date consistent with the OEB's guidelines.

RSL's Short Term Debt instruments are summarized below.

- Revolving Line of Credit: – RSL has access to a revolving line of credit facility in the amount of \$500,000 that is secured by a general security agreement over the Corporation's assets.
- Letter of Credit: – RSL has obtained a Letter of Credit from the Bank of Montreal in the amount of \$681,809 that has been issued in favour of the IESO. This Letter of Credit financially secures the Corporation's electricity purchases from the IESO, who has not drawn on this credit instrument.

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

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

Notional Debt

Notional debt is the portion of deemed debt that results from differences between the RSL's actual long term debt and the deemed debt of 60% of the rate base. With the planned loan in 2016, RSL's actual long-term debt will be within 60% of the deemed debt. Consistent with the Filing Requirement, RSL has applied the actual long term debt rate to the whole portion of deemed long term debt.

Not-For-Profit

Note that RSL is not a non-for-profit cooperation and as such, all requirements related to a not-for-profit organization do not apply.

Appendix

List of Appendices:

Appendix 5.1 - Promissory Notes

Appendix 5.1 – Promissory Notes

PROMISSORY NOTE

\$938,352.00

Date: October 31, 2000

For value received, the undersigned promises to pay on demand to the order of The Corporation of the Township of South Dundas, at its head office, the sum of Nine Hundred and Thirty-eight Thousand, Three Hundred and Fifty-two (\$938,352.00) Dollars.

This sum shall not bear interest from the date of the note to the earlier of the date of market opening or such time as the Directors shall decide.

Thereafter, interest is to be calculated with interest at a rate per annum as determined by the Directors from time to time, such amount not to exceed 7.25% per annum, or as negotiated annually. Interest shall be payable in the discretion of the Directors of the undersigned, taking into consideration the ability to pay of the undersigned (determined by the market value based rate of return phase in strategy, level of working capital or other reserves and the tax efficiency to shareholders of interest payments as opposed to dividend payments).

RIDEAU ST. LAWRENCE DISTRIBUTION INC.

Per: _____

I have authority to bind the Corporation.

PROMISSORY NOTE

\$225,000.00

Date: July 15, 2001

For value received, the undersigned promises to pay on demand to the order of The Corporation of the Village of Cardinal, at its head office, the sum of Two Hundred and Twenty-five Thousand (\$225,000.00) Dollars.

This sum shall not bear interest from the date of the note to the earlier of the date of market opening or such time as the Directors shall decide.

Thereafter, interest is to be calculated with interest at a rate per annum as determined by the Directors from time to time, such amount not to exceed 7.25% per annum, or as negotiated annually. Interest shall be payable in the discretion of the Directors of the undersigned, taking into consideration the ability to pay of the undersigned (determined by the market value based rate of return phase in strategy, level of working capital or other reserves and the tax efficiency to shareholders of interest payments as opposed to dividend payments).

RIDEAU ST. LAWRENCE DISTRIBUTION INC.

Per:  _____

I have authority to bind the Corporation