

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 Hydro
One Networks Inc. for an order approving or fixing
just and reasonable rates and other charges for the
distribution of electricity.

**REDACTED
ARGUMENT OF
CANADIAN MANUFACTURERS & EXPORTERS (“CME”)**

August 18, 2008

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I. INTRODUCTION & OVERVIEW

1. The 2008 test period is a Cost of Service re-basing year for Hydro One Networks Inc. ("Hydro One"). The Board's letter selecting Hydro One as one of the electricity distributors for re-basing in 2008 is dated May 4, 2007.¹ This letter followed Hydro One's letter to the Board dated November 3, 2006, requesting that it be included in the 2008 distribution rate group for a Cost of Service review.²
2. By the spring of 2007 and long before August 15, 2007, when Hydro One filed its Application in these proceedings, Hydro One knew that its revenue requirement and rates for 2008 would be determined on a Cost of Service basis. The last time Hydro One's rates were established on a Cost of Service basis was for its 2006 test year.³ In the Decision with Reasons for that case, which was issued on April 12, 2006, the Board approved a 2006 test year revenue requirement for Hydro One of \$965.2M.
3. The Board determined Hydro One's 2007 test year revenue requirement and rates by applying its 2nd Generation Incentive Regulation Mechanism ("IRM"). Hydro One's Board-approved revenue requirement for 2007 is \$969.6M, being an increase of about \$4.4M or about 0.4% over the Board-approved 2006 test year revenue requirement of \$965.2M.⁴
4. The evidence reveals that the Board's 2nd Generation IRM had no cost containment influence on Hydro One's spending in 2007. Hydro One's 2007 capital expenditures materially exceeded the capital budget and the capital spending covered by the Board-approved 2007 rates. As well, 2007 Operations, Maintenance and Administration ("OM&A") spending materially exceeded the amounts covered by the Board-approved 2007 rates. In Argument, Hydro One

¹ EB-2006-0330, Letter from the Ontario Energy Board, May 4, 2007

² EB-2006-0330, Letter from Hydro One to the Ontario Energy Board, November 3, 2006

³ EB-2005-0020

⁴ Ex.J1.7

heavily relies on its level of actual spending in 2007 as evidence demonstrating the reasonableness of its spending plans for 2008.⁵

5. There may have been some abnormal events in 2007 beyond Hydro One's control which contributed to its actual 2007 spending levels. However, the actual spending consequences of abnormal events should not influence the Board's determination of the reasonableness of Hydro One's spending plans for 2008. For regulatory purposes, prospective test year spending plans are to be based on assumptions that conditions during the test year will be normal, rather than abnormal. Spending levels in 2007 attributable to abnormal events are irrelevant to a determination of the reasonableness of Hydro One's spending plans for 2008.
6. It is important to recognize that, for 2007, the Board approved only the increase in revenue requirement produced by 2nd Generation IRM. There is no Board-approved 2007 OM&A budget. The Board did not approve a specific amount for Hydro One's 2007 OM&A costs. However, in determining the reasonableness of Hydro One's 2008 OM&A budget it is appropriate to consider the level of OM&A spending the Board would likely have approved for 2007 had it considered the issue on a cost of service basis having regard to Hydro One's actual 2006 OM&A costs. Hydro One's actual 2006 OM&A costs were \$404.1M⁶, which is \$19M or 4.7% less than the Board-approved 2006 OM&A budget of \$423.1M.⁷ Further, the actual 2006 OM&A costs of \$404.1M included some abnormally higher than expected amounts because of the unusually high frequency and intensity of storms in 2006. In these circumstances, the actual 2006 OM&A spending, to be considered as a bridge year to a 2007 OM&A budget, would be lower than \$404.1M because the OM&A budget for regulatory purposes should be based on normal conditions.

⁵ Argument-in-Chief of Hydro One, Transcript Volume 7, July 22, 2008, pp. 15-16

⁶ Ex.C1-2-1, p. 2

⁷ Ex.H-10-16, p. 3

7. We submit that, in these circumstances, the primary comparator which the Board should use in determining the 2008 OM&A budget is Hydro One's 2006 actual OM&A costs of \$404.1M unadjusted for any higher than anticipated costs attributable to abnormal events. The unadjusted 2006 actual OM&A costs, we submit, are a reasonable surrogate for the 2007 OM&A budget the Board would likely have approved for Hydro One had it considered the issue on a cost of service basis in the context of Hydro One's actual 2006 spending. It is noteworthy that Hydro One's witnesses agree that the 2006 actual costs provide a good historical base for assessing the reasonableness of amounts which it asks the Board to approve in this proceeding.⁸
8. Hydro One's contention that all of its over-spending in 2007 was motivated by public interest considerations should be viewed with some scepticism in the context of the reality that Hydro One had requested, in November 2006, and knew, by the spring of 2007, that its revenue requirement and rates for 2008 would be determined on a Cost of Service basis.
9. In this connection, CME submits that an anticipated transition to incentive regulation influences budgeting. Utilities can view re-basing as an opportunity to seek approval of a revenue requirement that substantially exceeds the revenue requirement which would be produced by continuing to apply the IRM. During the 2007 and 2008 budget processes, the knowledge that the 2008 Test Year would be used as the base-year for 3rd Generation IRM has a tendency, whether intentionally or unintentionally, to induce increased budgets. This phenomenon, in combination with bridge year over-spending will, we submit, inevitably lead to over-budgeting in the test year, that, in this case, is also the base-year for 3rd Generation IRM.

⁸ Transcript Volume 2, July 8, 2008, p. 42

10. Accordingly, when assessing the reasonableness of the increases requested by Hydro One, the Board should not lose sight of the fact that bridge year overspending, in combination with the expected transition from Hydro One's 2008 Distribution Rates Application to 3rd Generation IRM in 2009, tends to inflate test year budget amounts, which in turn, will enhance Hydro One's opportunity to earn more than the board-allowed return during IRM. In this context we urge the Board to scrutinize, with care, the excessive 2007 overspending upon which Hydro One relies to justify the 2008 revenue requirement it seeks in this application. The Board should ascribe little, if any, weight to Hydro One's 2007 overspending when evaluating the reasonableness of the 2008 revenue requirement. There is, we submit, a significant tactical component to the 2007 overspending as is evident from Hydro One's reliance on it to request an unreasonably high revenue requirement and rates for 2008, which, in turn, become the point of departure for the approval of Hydro One rates for 2009, 2010 and 2011 under the auspices of the Board's 3rd Generation IRM.
11. When considering the reasonableness of the overall 2008 revenue requirement proposed by Hydro One, we urge the Board to consider the amount requested, compared to the revenue requirement that would have been produced had Hydro One's revenue requirement for 2008 been determined by applying the escalation factor which the Board's 2nd Generation IRM produces. Had Hydro One continued to operate under the 2nd Generation IRM in 2008, its revenue requirement would have been \$982.3M.⁹ This is an increase of \$17.1M from 2006 to 2008, and would have represented a 1.7% increase over two years.
12. In the current application, Hydro One requests Board approval of a total revenue requirement of \$1,066.8M for its 2008 distribution rates.¹⁰ This revenue requirement is \$84.5M more than the \$982.3M revenue requirement that would

⁹ Ex.J1.7

¹⁰ Ex.E-2-1-1

have been produced under 2nd Generation IRM. Put another way, the 2008 revenue requirement Hydro One requests is almost six (6) times greater than the \$17.1M increase that 2nd Generation IRM would have produced.

13. The revenue requirement increase of \$84.5M represents an 8.7% increase in the Board approved revenue requirement for 2007 of \$969.6M. We submit that this level of revenue requirement increase is materially incompatible with the escalation factors recently approved by the Board. As set out above, this level of increase is materially greater than the escalation factor produced by 2nd Generation IRM. It is also materially greater than the escalation factors recently approved by the Board for Union Gas Limited ("Union") and Enbridge Gas Distribution ("EGD").¹¹ For Union's 2008 Price Cap IRM, the 2008 escalation factor is 0.22%, being the difference between Canada's Gross Domestic Product Implicit Price Index Final Domestic Demand ("GDP IPI FDD"), for 2008 of 2.04%, and the agreed upon X Factor of 1.82%. Union's 2008 escalator is about 10% of the rate of inflation. For EGD's 2008 Revenue per Customer Cap IRM, the 2008 escalation factor is 1.22%, being the 2008 GDP IPI FDD of 2.04% reduced by an agreed upon X Factor of 40% of GDP IPI FDD (this produces an X Factor of 0.816% for 2008). For 2009 and 2010 EGD's X Factor will increase to 45% of GDP IPI FDD. For 2011 EGD's X Factor will increase to 50% of GDP IPI FDD and in 2012 EGD's X Factor will increase to 55% of GDP IPI FDD. Thus, for the period 2008-2012, the escalation factor for EGD's Revenue per Customer Cap IRM will remain well below the rate of inflation.
14. We further submit that an 8.7% year-over-year increase in revenue requirement, in and of itself, raises excessiveness concerns and CME's submissions, which follow, focus on the components of Hydro One's 2008 revenue requirement which we submit are excessive.

¹¹ January 17, 2008 Decision in EB-2007-0606 and February 11, 2008 Decision in EB-2007-0615

15. Because many of the issues which the Board listed for determination during these proceedings were either settled or partially settled, as described in the Settlement Proposal which the Board approved on or about June 19, 2008, we have not organized CME's Written Argument by using each of the unresolved issues as a topic heading. Rather, CME's Written Argument is organized under the following major topic headings:
- (a) Appropriate Regulatory Treatment for Smart Meters;
 - (b) Rate Base;
 - (c) Excessiveness of the Components of and the Overall Level of the OM&A Budget;
 - (d) Regulatory Assets Refund;
 - (e) Conservation Demand Management ("CDM") Budget;
 - (f) Lost Revenue Adjustment Mechanism ("LRAM");
 - (g) Cost Allocation and Rate Design;
 - (h) Deferral and Variance Accounts; and
 - (i) Costs.
16. In the course of preparing this Written Argument, CME has discussed the unresolved matters in issue with AMPCO, CCC, Energy Probe, SEC, and VECC. The purpose of these discussions was to reduce or eliminate, where possible, the duplication of similar submissions from ratepayer representatives on matters of common interest. As a result of these discussions, we are aware of the positions that these intervenors intend to take in Argument with respect to issues of interest to CME. Throughout this argument we have attempted to identify the positions of other intervenors that CME adopts and supports.

II. APPROPRIATE REGULATORY TREATMENT FOR SMART METERS

17. CME takes no position on Hydro One's proposed Smart Meter budget, including costs that exceed "minimum functionality", because, by and large, these costs do not directly impact CME members. CME does, however, have concerns about the proposed regulatory treatment of Smart Meter costs. As the regulatory treatment proposed by Hydro One may have an impact on the overall revenue requirement increases under 3rd Generation IRM, it could impact CME members.
18. Hydro One has requested that all Smart Meter costs be approved for recovery as a regulatory asset up to April 30, 2008, and then be included in its core work program beyond that time for recovery as part of its revenue requirement. In CME's view, Smart Meter costs should be regulated on a "pass-through" basis in accordance with the approach most recently approved in the Toronto Hydro-Electric System Limited Rates Case ("Toronto Hydro Case").¹² For this reason, the Board should direct Hydro One to continue the current smart meter regime whereby costs are funded through a smart meter adder with a variance account mechanism to enable subsequent true ups. This is the
19. The rationale for continuing the current regime was set out by the Board in the Toronto Hydro Case as follows:

"While the Board accepts that the Company is now in a better position to forecast its costs associated with smart meters, the Board is of the view that there is still considerable risk that the Company's forecasts may be substantially off the mark, resulting in significant over- or under-recovery. The issue is not necessarily that smart meter installation expenditures may not materialize; rather, the concern is the potential of timing differences in the actual expenditures from those forecasts. Timing differences will always exist, however, neither the Utility nor ratepayers should benefit or be burdened by an initiative that is temporal in nature and can be reasonably viewed as a cost pass-through. Treating smart meter expenditures for rate making purposes like any other core distribution activity is premature. The Board sees no harm in permitting the current regime to continue as it offers protection for both the

¹² EB-2007-0680

Company and ratepayers from the vagaries of missed forecasts. As the installation program progresses and once the Board has reviewed and approved actual expenditures, bringing these expenditures into rate base can be considered again.”¹³

20. There is no reason why Hydro One’s Smart Meter costs should be treated differently than Toronto Hydro’s Smart Meter costs. In this regard, during the Hearing, Hydro One’s counsel acknowledged as follows:

“It is their [Hydro One] preference that that is the treatment that be given to them, but it has since become aware of the Toronto Hydro decision and I have no – I can give you no rationale why my client should be treated differently from Toronto Hydro”.¹⁴

21. For the reasons set out above, CME requests that the Board direct Hydro One to continue to fund its Smart Meter costs through a smart meter adder, and maintain a deferral account to track smart meter costs.

III. RATE BASE

22. The Rate Base item that CME questions pertains to the appropriateness of including a \$28M capital expenditure for the Cornerstone project without concurrently ensuring that an appropriate amount of ensuing cost savings will be allocated to ratepayers.¹⁵ CME does not oppose the \$28M capital expenditure so long as an appropriate amount of the cost savings are attributed to ratepayers either now or during the forthcoming IRM period.
23. Hydro One has forecast cost savings equal to \$200M over the period of 2009 to 2015.¹⁶ Of the total \$200M of cost savings, \$59M is attributed to distribution¹⁷ and the remaining \$141M is attributed to transmission. Over the next three years,

¹³ EB-2007-0680, Decision of the Board, May 15, 2008, pp. 24-25

¹⁴ Transcript Volume 2, July 8, 2008, p. 70; see also Argument-in-Chief of Hydro One, Transcript Volume 7, July 22, 2008, p. 25

¹⁵ Ex.D1-3-5, p. 16

¹⁶ Ex.D1-3-5, p. 21

¹⁷ Transcript Volume 3, July 10, 2008, pp. 86-87

which is the expected period for 3rd Generation IRM, the Cornerstone project will result in \$23M in savings.¹⁸ Unless the Board provides a mechanism to capture those savings, Hydro One's shareholder will benefit from the savings even though ratepayers paid the carrying costs of the capital expenditure in 2008. In this regard, when asked by Board Staff how Hydro One intends to capture the cost savings during IRM, Hydro one responded that "Hydro One assumes any savings beyond 2008, specifically for 2009 and 2010, will be captured under the Board's approved 3rd Generation IRM."¹⁹

24. In CME's view, the "matching of costs and benefits" principle calls for the adoption of a mechanism to ensure that an appropriate amount of the cost savings are attributed to ratepayers either now or during IRM. Hydro One's shareholder should not experience a windfall of cost savings during an IRM period from a project funded during the rebasing year.

IV. EXCESSIVENESS OF THE COMPONENTS OF AND THE OVERALL LEVEL OF THE OM&A BUDGET

25. In CME's view, the OM&A increases that Hydro One seeks in this application are excessive. This is demonstrated by a global or envelope comparison of Hydro One's overall 2008 OM&A Budget compared to its 2006 actual OM&A costs, and by an analysis of the various subcomponents that comprise the overall OM&A Budget.
26. As set out above, 2006 was the last year that Hydro One's OM&A budget was subject to a cost or service application. While the Board approved a 2006 total OM&A budget of \$423.1M²⁰, Hydro One's actual 2006 OM&A costs were

¹⁸ Ex.J3.7
¹⁹ Ex.H-1-38, p. 5
²⁰ Ex.H-10-16, p. 3

\$404.1M.²¹ For the reasons we have previously articulated, the primary comparator the Board should use to assess the reasonableness of Hydro One's proposed 2008 OM&A costs is Hydro One's actual 2006 OM&A costs.

27. We are aware that several intervenors including AMPCO, SEC and VECC will be making detailed submissions with respect to the excessiveness of a number of the line item components of Hydro One's proposed 2008 OM&A budget. CME adopts and supports those submissions and relies upon the excessiveness in the various line item components of the Budget to support a global reduction in the total 2008 OM&A Budget in an amount of at least \$44.8M. We derive this suggested disallowance amount by applying an envelope approach in the manner described in the paragraphs of this Argument that follow.
28. In particular, we support and adopt the following:
- (a) The submissions of SEC, VECC and AMPCO pertaining to Hydro One's proposed Sustaining OM&A Budget, including the excessiveness of the Vegetation Management Budget;
 - (b) The submissions of SEC pertaining to the excessiveness of Hydro One's proposed Asset Management Costs;
 - (c) The submissions of SEC and VECC with respect to the excessiveness of Hydro One's proposed Human Resources Costs; and
 - (d) The submissions of VECC pertaining to the excessiveness in the Cost of Living Adjustment ("COLA") as applied in the Inergi Contract.
29. The excessive line item amount which we address in this Argument is the 2008 OM&A budget item for Shared Services and Other OM&A. Hydro One's actual 2006 Shared Services and Other OM&A costs were \$21.2M²², compared to

²¹ Ex.C1-2-1, p. 2

²² Ex.C1-2-1, p. 2

Hydro One's Board-approved 2006 Shared Services and Other OM&A budget of \$67.9M. In this case, Hydro One requests approval of a 2008 Shared Services and Other OM&A budget of \$66.9M, which is \$45.7M greater than Hydro One's Actual 2006 Shared Services and Other OM&A costs of \$21.2M.²³ While CME recognizes that part of this increase relates to the Hydro One's 2006 deferred pension credit²⁴, this tripling of Shared Services and Other OM&A costs from \$21.2M in 2006 to \$66.9M in 2008 nevertheless calls for careful scrutiny by the Board.

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31. This Board has confirmed, in prior cases, the importance of obtaining independent evaluations to justify increases in the amount of allocated corporate costs over those actually incurred in 2006.²⁶ The absence of an up-to-date independent study to support the increases sought prompts CME to ask whether Hydro One has justified the requested increase.

²³ Ex.C1-2-1, p. 2

²⁴ Ex.C1-2-6, p. 81

²⁵

²⁶ EB-2005-0001, pp. 77 and 78

32. There is no independent study supporting the increases sought by Hydro One. Hydro One relies upon a study conducted by R.J. Rudden in the 2006 Distribution Case.²⁷ This study is out of date. In particular, Hydro One has not:
- (a) Had R.J. Rudden assess whether their 2006 methodology has been properly applied to Hydro One's 2008 budget;
 - (b) Asked an independent expert to assess the prudence of the increase from 2006 Actuals to 2008 Budget; or
 - (c) Undertaken an up-to-date external study or internal study on the economies of scale, if any, that are being achieved through Hydro One's shared services.²⁸
33. There is no independent evidence to justify the 2008 Shared Services and Other OM&A budget increase Hydro One requests over the actual 2006 Shared Services and Other OM&A costs. On the authority of EB-2005-0011, the increase in the Shared Services and Other OM&A category should be disallowed.
34. This disallowance would reduce Hydro One's total 2008 OM&A budget by \$45.7M from \$477.7M to \$432M. If the costs of the Smart Meter Program are removed from Hydro One's proposed 2008 OM&A budget, then a disallowance of \$45.7M would reduce Hydro One's 2008 OM&A budget from \$468M to \$422.3M.²⁹ A 2008 OM&A budget \$432M, which includes the Smart Meter Program, represents an increase of \$27.9M over the actual 2006 OM&A costs of \$404.1M, or an increase of 6.9% over two years. A 2008 OM&A budget \$422.3M, which excludes the Smart Meter Program, would represent an increase of \$23.1M over the \$399.2M actual 2006 OM&A costs excluding the Smart Meter Program, or an increase of 5.7% over two years.

²⁷ Ex.C1-2-6

²⁸ Transcript Volume 1, pp. 27-33

²⁹ Ex.J2.2

35. CME is not requesting that the Board reduce Hydro One's 2008 OM&A budget on a line-by-line basis. Rather, CME urges the Board to consider the excessiveness in individual budgeted 2008 OM&A categories when determining an overall global or envelope reduction. The Board may consider that the proposed 2008 Shared Services and Other OM&A budget, as an example, has tripled over the actual Shared Services and Other OM&A expenditures in 2006. CME also urges the Board to consider the line-by-line assessment of OM&A budget increases conducted by AMPCO, SEC and VECC, and in particular, their submissions on the excessiveness of the Vegetation Management Budget, the Asset Management budget and Hydro One's proposed Human Resources Costs.
36. In Hydro One's 2006 Distribution Rates Case, the Board did not rely upon a global or envelope assessment of the reasonableness of Hydro One's OM&A costs because, at that time, there did not exist a solid historical baseline. In this regard, the Board stated as follows:

*"3.2.3 In the Board's view, while global or envelope reductions to costs proposed by a utility can be and have served as a practical tool in other circumstances, this approach is not appropriate in this case. It is true, given the history of regulation of Hydro One, and its anomalous nature, that there is no solid historical baseline to compare the proposed costs."*³⁰

37. In that case, the Board also recognized that Hydro One's 2006 Distribution Rates Case would establish a historical baseline upon which the Board could rely upon in future rates cases. The Board stated as follows:

*"3.2.7 By way of general comment, while this first review of Hydro One's OM&A Budget proved daunting for the intervenors and the Board, it is the Board's view that this proceeding has provided a good base for future examination of OM&A costs, which will permit a more rigorous assessment of OM&A costs in the future."*³¹

³⁰ EB-2005-0020

³¹ EB-2005-0020

38. We reiterate that Hydro One's witnesses agree that the 2006 actual costs, in general, provide a good historical base for assessing the reasonableness of the amounts claimed in this proceeding.³²
39. In its Argument-in-Chief, Hydro One attempts to downplay the value of using percentage comparisons to assess the reasonableness of the OM&A costs claimed in the current application. Counsel for Hydro One stated as follows:

*"As the Board will have observed, Intervenors are fond of seeking percentage comparisons and selected categories of costs would show large increases over a several year period. This is designed to create the impression that costs are escalating in leaps and bounds."*³³

40. Compared to its actual 2006 OM&A costs of \$399.2³⁴, excluding the Smart Meter Program, Hydro One's costs, in fact, are escalating by leaps and bounds. This is not an illusion created by the creative use of percentage comparisons. The percentage increases of Hydro One's proposed 2008 OM&A budget compared to its 2006 actual OM&A costs, which followed Hydro One's last distribution rate cost of service application, is appropriate. Such a comparison is a useful tool for the Board to assess whether Hydro One's OM&A costs have been kept within the limits of reasonableness since 2006.
41. The determination of the 2008 OM&A costs to be recovered in rates is an exercise of judgment that the Board must make after considering all factors which it regards as relevant. One of the tools we urge the Board to use when making this judgment include a comparison of the budgeted 2008 OM&A costs to Hydro One's actual 2006 OM&A costs. Such a comparison shows that Hydro One has not contained its OM&A costs within the limits of reasonableness since 2006. This type of global or envelope approach to evaluating the reasonableness

³² Transcript Volume 2, July 8, 2008, p.42

³³ Transcript Volume 7, July 22, 2008, p. 16

³⁴ Ex.J2.2

budget claims is an established approach that this Board has approved in prior cases, including in Hydro One's 2006 Electricity Distribution Rates Case.

42. Hydro One requests approval of a 2008 OM&A Budget of \$477.7M.³⁵ This is a \$73.6M increase over Hydro One's 2006 actual OM&A costs of \$404.1M.³⁶ If approved, this would represent an 18% increase over two years.
43. CME acknowledges that a portion of this increase is attributable to Smart Meters. However, even when the costs of the Smart Meter Program are removed, the increase in the OM&A Budget remains excessive. Hydro One's OM&A costs in 2006, excluding the Smart Meter Program, were \$399.2M.³⁷ Hydro One is seeking Board approval of an OM&A Budget, excluding the Smart Meter Program, of \$468M.³⁸ This is an increase of \$68.8M which represents a 17.2% increase over two years.
44. CME submits that the factors that the Board should consider in measuring the reasonableness of a budget increase in excess of 17% over two years include the following:
 - (a) The extent to which this overall percentage increase exceeds the percentage escalation factor which the Board-approved 2nd Generation IRM produces. This escalation factor provides an indication of the percentage level year-over-year increase which is reasonable;
 - (b) The extent to which this overall percentage increase exceeds the percentage escalation factors recently approved by the Board for Union and EGD;

³⁵ Ex.C1-2-1, p. 2

³⁶ Ex.C1-2-1, p. 2

³⁷ Ex.J2.2

³⁸ Ex.J2.2

- (c) The level of increase in Hydro One's OM&A cost per customer from 2006 to 2008;
 - (d) The level of increase in Hydro One's OM&A per circuit km of distribution lines from 2006 to 2008; and
 - (e) The extent to which the percentage increase of OM&A costs over 2 years exceeds the increase over two years in the rate of inflation.
45. Hydro One continued to operate under 2nd Generation IRM in 2008, its revenue requirement would have been \$982.3M.³⁹ This revenue requirement increase reflects an escalation factor of 1.7% for the 2006 to 2008 period. The OM&A Budget increase which Hydro One seeks to have the Board approve in this case, excluding the Smart Meter Program, is over 17% over two years or 10 times greater than the escalation factor produced by 2nd Generation IRM for the 2006-2008 period.
46. As set out above, the incentive regulation adjustment mechanisms which the Board recently approved for Union and EGD's IRM are another source of information we urge the Board to consider when evaluating the reasonableness of the percentage increase Hydro One's 2008 OM&A budget compared to its 2006 actual OM&A costs.⁴⁰ These Board-approved adjustment mechanisms contained an annual inflation rate of approximately 2%, from which is deducted a productivity factor that reduces the overall adjustment factor to produce a percentage increase less than 2% per year.
47. This Board has recognized that, in terms of a global approach, it is appropriate to look at the OM&A cost per customer, which is a measure that permits the Board to review cost levels and trends over time while taking into account customer

³⁹ Ex.J1.7

⁴⁰ EB-2007-0606 and EB-2007-0615

growth.⁴¹ Hydro One's total 2006 OM&A per customer was \$350.⁴² For 2008, Hydro one's proposed OM&A budget, if approved, would increase the OM&A by \$54 to a total of \$404 per customer.⁴³ This is a 15.4% increase in the cost of OM&A per customer over two years. CME urges the Board to consider this increase of OM&A on a per customer basis as further evidence that Hydro One's proposed 2008 OM&A budget is not within the limits of reasonableness.

48. CME submits that another factor the Board should consider is Hydro One's proposed 2008 OM&A budget increase on a per circuit km of distribution lines basis ("per circuit km"). This measure allows the Board to assess Hydro One's proposed 2008 OM&A budget while taking into account growth in Hydro One's distribution lines. In 2006, Hydro One's total OM&A cost per circuit km was \$3,372.⁴⁴ If Hydro One's proposed 2008 OM&A budget is approved, Hydro One's OM&A cost per circuit km will increase by \$601 to \$3,973 OM&A per circuit km.⁴⁵ This is an increase of 17.8% over two years. This two year increase further supports CME's position that Hydro One's total 2008 OM&A budget should be subject to a global or envelope reduction.
49. Over the period 2006 to 2008, at a rate of inflation at 2% per year, the total expected inflation increase is about 4%. The OM&A Budget for which Hydro One seeks Board approval, excluding the Smart Meter Program, is more than four times greater than a 4% inflation increase over the 2006-2008 period.
50. CME urges the Board to consider all of these factors and to disallow a significant portion of the overall 2008 OM&A Budget sought by Hydro One. In determining the proper amount to disallow, CME submits that a reasonable range of percentage increase from Hydro One's 2006 actual OM&A costs is between

⁴¹ EB-2005-0001, pp. 94-98

⁴² Ex.H-1-59

⁴³ Ex.H-1-59

⁴⁴ Ex.H-1-59

⁴⁵ Ex.H-1-59

1.7% [which is the percentage increase produced by 2nd Generation IRM] and 6% [which is 150% of the rate of inflation over two years of 4%]. Applying these ranges, Hydro One's 2008 OM&A budget, excluding the Smart Meter Program, should be between \$406M and \$423.2M. This represents a disallowance of Hydro One's requested OM&A budget, excluding the Smart Meter Program, of between \$44.8M and \$62M. CME urges the Board to find that the total budgeted 2008 OM&A budget is excessive by at least \$44.8M, which is the lower limit of the range of reasonableness. We urge the Board to approve a 2008 OM&A budget, including the Smart Meter Program, of about \$432M.

V. REGULATORY ASSETS REFUND

51. CME supports Hydro One's request to dispose of regulatory asset balances up to April 30, 2008 in the amount of \$65.5M.⁴⁶
52. The lack of an audit for the period of January 1, 2008 to April 30, 2008 should not preclude disposal of this account at this time. A true up, if required, could be made at a later date. In CME's submission, there is no reason why the regulatory asset balance should not be disposed of in the manner proposed by Hydro One, particularly given the fact that it will mitigate the customer impacts that arise out this application.
53. As a general rule, CME sees no reason to phase-in the payback of regulatory asset balances owing to ratepayers. For this reason, the amount of \$65.5M should be paid back over a duration approximately equivalent to the time it took for the amount to accumulate.

⁴⁶ Ex.F1-1-1; Ex.J6.2

VI. CONSERVATION DEMAND MANAGEMENT (“CDM”) BUDGET

54. CME understands that Pollution Probe and/or GEC will be asking the Board direct Hydro One to increase its CDM budget by approximately \$15M in order to carry out CDM activities regardless of OPA funding.
55. Hydro One supports the Ontario Government’s CDM target to achieve a 1350 MW of peak reduction by 2007 and a further reduction of 1350 MW by 2010.⁴⁷ In this regard, Hydro One used the Board approved third tranche funding of \$39.5M to cover its CDM programs for the 2004 to 2007 period. Once the third tranche funding expires, Hydro One will then rely on the CDM funding from OPA to fund its CDM initiatives in 2008 and beyond.⁴⁸ CME supports Hydro One’s reliance on the CDM funding from OPA.
56. Currently, Hydro One is participating in all of the OPA core programs available for all LDCs. Hydro One has also been working with OPA staff to develop programs to be funded by OPA for 2008.⁴⁹ In this regard, Hydro One has made custom applications to the OPA for demand management programs to Hydro One’s General Service (“GS”) customers as well as sub-transmission customers.
57. The OPA is responsible for delivering the CDM target for the province, and Hydro One has confirmed that it will be working closely with OPA. Hydro One has confirmed that it will be working with OPA staff to come up with proposals not only for the test year, but also for future years. That said, it is the OPA – and not Hydro One - that decides effectively how much money will be available for each program and for each LDC.
58. It is not Hydro One’s role to assess, on a province-wide basis, the best manner to carry out CDM. This is the role of OPA. CME agrees with Hydro One that the

⁴⁷ Ex.A-14-3, p. 8

⁴⁸ Transcript Volume 4, July 15, 2008, pp. 142-143

⁴⁹ Transcript Volume 4, July 15, 2008, p. 130

OPA is the best agency to coordinate the CDM effort province wide and that it is not appropriate to ask its customers to fund additional CDM in 2008 beyond what is provided by the OPA.⁵⁰ We submit that the Board should not direct Hydro One to increase its CDM activity beyond OPA funded programs.

VII. LOST REVENUE ADJUSTMENT MECHANISM (“LRAM”)

59. A LRAM can be a valuable regulatory tool. This has been demonstrated by EGD and Union’s use of LRAMs in relation to their respective Demand Side Management programs. That said, for a LRAM to be effective the utility must have access to the information needed to determine, with certainty, the impact that utility’s conservation programs.
60. Unlike EGD and Union, Hydro One faces major gaps in critical information required for the proper operation of the LRAM. As set out by Hydro One’s witness, Mr. But, Hydro One has not put forth a LRAM proposal in this application because critical Evaluation, Measurement and Verification (“EMV”) information is not available from the OPA.⁵¹ Furthermore, Hydro One is also missing EMV results pertaining to non-OPA programs initiated by other entities such as the federal and provincial governments.
61. With respect to the information gap which precludes the implementation of a LRAM, at this time, this Board recently concluded in the Toronto Hydro case as follows:

“In a number of utility applications for rates in 2008, the specific effect of CDM activities on throughput has been impossible to quantify with any reasonable degree of accuracy. This means that an important area of public policy, supported by considerable funding through distribution delivery rates, as well as through direct OPA program funding under the

⁵⁰ Transcript Volume 4, July 15, 2008, pp. 142-143

⁵¹ Transcript Volume 4, July 15, 2008, pp. 9-10

*global adjustment, is not measurable according to a consistent and well understood methodology. This lack of alignment between the OPA forecasts and those generated by individual utilities also has implications for LRAM and SSM claims and calculations. LRAM and SSM claims are limited to the demonstrable effects of the specific utility's CDM programs on its throughput and revenue. In order to make this assessment, such effects must be empirically accounted for. The effects of CDM activities that are not attributable to the specific utility's actions must also be definitively accounted for."*⁵²

62. The success of an LRAM is dependent on the availability of fulsome EMV information. While OPA is working to improve its EMV information, but at this time the information required by Hydro One to effectively implement a LRAM is not available. Without that necessary evidence, it is not appropriate to implement a LRAM. For this reason, CME does not believe that it is appropriate for the Board to direct Hydro One to implement a LRAM, on inadequate information, for 2008.

VIII. COST ALLOCATION & RATE DESIGN

A. Summary of Hydro One's Proposal

63. Hydro One's Cost Allocation and Rate Design proposal can be summarized as follows:
- (a) Reduce the 280 existing customer classes to 12 new customer classes;
 - (b) Apply the Board-approved Cost Allocation methods to allocate costs to the new rate classes, subject to certain exceptions which Hydro One asks the Board to approve;
 - (c) Establish "end-state" rate levels at revenue-to-cost ratios for each customer class which are compatible with OEB revenue-to-cost ratio guidelines;

⁵² EB-2007-0680, Decision of the Board, May 15, 2008, p. 33

- (d) Confine the impact on existing customers of the “end-state” rates to an examination of their impact on an “average” customer within each class;
- (e) Rebalance existing rates over four (4) years so that the bill impact on an average customer within each class is no more than 10% per year; and
- (f) Terminate the interim Time-of-Use (“TOU”) Program approved by the Board by Order dated November 24, 2004.⁵³

64. CME’s submissions with respect to each of these proposals are organized under the following topic headings:

- New Customer Rate Classes
- Cost Allocation
- “End-State” Revenue-to-Cost Ratios
- “End-State” Rate Impact Measurement
- Rate Re-Balancing Transition
- Termination of Interim TOU Program

B. New Customer Rate Classes

65. We understand that counsel for SEC and perhaps others will be urging the Board to find that Hydro One has failed to objectively demonstrate the appropriateness of the demarcation points in its proposed density based re-classification of existing General Service rate classes. The lack of empirical support for its General Service rate re-classification proposals may well prompt the Board to refrain from approving, at this time, the General Service rate re-classifications Hydro One proposes. CME supports rate harmonization and its argument with respect to the new customer rate classes Hydro One proposes proceeds from

⁵³ RP-2004-0203/EB-2004-0457

the premise that, as a pragmatic matter, there will eventually be a material reduction in the 280 rate classes that currently exist.

66. Regardless of the rate re-classification and harmonization process that the Board either approves or directs Hydro One to apply, a priority issue will be a determination of the rate and bill impacts of such measures on those ratepayers who will be most adversely affected by the re-classification and harmonization proposals.
67. Our submissions with respect to new customer rate classes and the other topics pertaining to Hydro One's Cost Allocation and Rate Design proposals apply to whatever customer classification model the Board approves or directs Hydro One to adopt in this particular case.
68. Accordingly, for the purposes of its submissions which follow, CME proceeds from the premise that Hydro One's existing 280 rate classes will eventually be materially reduced.
69. For the purposes of its submissions, CME recognizes that some refinements to the description of the new customer classes proposed by Hydro One may be appropriate such as refinements of the type AMPCO proposes for the Sub-Transmission ("ST") customer class. CME also recognizes that the Board might direct Hydro One to conduct further analysis to support a definition of the new Urban General Service rate class in a further proceeding confined, in scope, to Rate Design matters.
70. CME takes no position on the issue of whether or not there should be a separate customer class for Unmetered Scattered Load ("USL") as Rogers Cable proposes.

71. CME relies on the Board to apply its expertise in determining whether there is any persuasive rationale for changing the method of billing for shared feeders from the “per kilometer” basis currently applied to the “per kilowatt” basis proposed by Milton Hydro.
72. A point not expressly addressed during oral hearing but one which occurred to us during the preparation of argument is the question whether the 12 new customer classes Hydro One proposes are compatible with the new rate classifications currently under discussion in the Rate Design for Recovery of Electricity Distribution Costs Consultative (the “Consultative”).⁵⁴ We suggest that an effort should be made in this proceeding to avoid approving new customer classifications which are materially incompatible with customer classes under consideration in the Consultative. We make this suggestion recognizing that, in its submission in the Consultative, Hydro One suggests that level of transformation is a more logical differentiation for grouping customers than connection voltage. Nevertheless, we submit it would be helpful for the Board to know whether the new customer classifications Hydro One proposes will accommodate a smooth transition to either voltage-based or transformation-based customer classes that may be adopted at the conclusion of the Consultative.⁵⁵
73. We have examined the compatibility of the customer classes Hydro One proposes with those under discussion in the Consultative and our comparison of these customer classifications is shown on Table 1 below:⁵⁶

⁵⁴ EB-2007-0031

⁵⁵ Comments of Hydro One dated May 20, 2008

⁵⁶ EB-2007-0031 Staff Discussion Paper dated March 31, 2008; Comments by CME dated May 30, 2008; Ex.G1-2-3

TABLE 1

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Board Staff's Proposed Customer Classifications	Description	CME's Re-Labeling of Board Staff's Proposed Customer Classifications	Board Staff's Proposed Customer Classifications	Hydro One's EB-2007-0681 Proposed Customer Classifications
Single Phase Secondary Class	<ul style="list-style-type: none"> • Almost all residential customers • Significant portion of customers in General Service < 50 Kw • Few customers in General Service > 50 kW 	Low Voltage Distribution Customers	Single Phase Secondary Class	<ul style="list-style-type: none"> • Urban Residential (High Density) • R1 Residential (Medium Density) • R2 Residential (Low Density) • Urban General Service energy billed • Urban General Service demand billed • General Service energy billed • General Service demand billed • Distributed Generation?
Three Phase Secondary Class	<ul style="list-style-type: none"> • Few residential customers • Significant portion of customers in General Service < 50 kW • Most customers in General Service > 50 kW 	Medium Voltage Distribution Customers	Three Phase Secondary Class	<ul style="list-style-type: none"> • Urban General Service energy billed • Urban General Service demand billed • General Service energy billed • General Service demand billed • Seasonal • Distributed Generation?
Primary Class	<ul style="list-style-type: none"> • General Service > 50 kW 	Intermediate/High Voltage Distribution Customers	Primary Class	<ul style="list-style-type: none"> • Urban General Service energy billed • Urban General Service demand billed • General Service energy billed • General Service demand billed • Distributed Generation?
Sub-transmission Class	<ul style="list-style-type: none"> • Over 1000 kW demand 	High Voltage Distribution Customers	Sub-transmission Class	<ul style="list-style-type: none"> • Sub-transmission • Distributed Generation?
Embedded Distributors	<ul style="list-style-type: none"> • Electricity Distributor provided electricity by means of host distributor facilities 	Embedded Distributors	Embedded Distributors	<ul style="list-style-type: none"> • Distributed Generation?
Load Displacement Generation	<ul style="list-style-type: none"> • Generation facilities that supply electricity to specific load 	Load Displacement Generation	Load Displacement Generation	<ul style="list-style-type: none"> • Distributed Generation?
Unmetered Scattered Load	<ul style="list-style-type: none"> • Street lighting • Sentinel lighting • Cable facilities 	Unmetered Multi-Load Distribution Customers - Street/Sentinel Lighting, and Cable Facilities	Unmetered Scattered Load	<ul style="list-style-type: none"> • Street Light • Sentinel Light
Metered Scattered Load	<ul style="list-style-type: none"> • School boards, municipalities, universities and hospitals 	Aggregate Multi-Load Distribution Loads	Metered Scattered Load	

74. We invite Hydro One to address, in its Reply Argument, whether any of the new customer classes it proposes are materially incompatible with customer classes under consideration in the Consultative.

C. Cost Allocation

75. We agree that the Board-approved Cost Allocation methods should be applied to allocate Hydro One's Cost of Service and Return to the new rate classes.
76. The evidence indicates that, with a few exceptions, Hydro One has applied these Cost Allocation methods. The Cost Allocation methodology exceptions, which Hydro One ask the Board to approve in this case, pertain to the provision of ST service to embedded customers, the application of density weights to reflect the primary rural nature of Hydro One's system, and the large number of customer classes.⁵⁷ We recognize that SEC will be challenging aspects of the exceptions to the approved Cost Allocation methods which Hydro One asks the Board to approve in this case. In particular, we are aware that SEC has legitimate reasons for challenging the density-based customer classifications and allocation factors Hydro One has developed.⁵⁸
77. We rely on the Board to apply its expertise to determine whether the exceptions and/or refinements Hydro One has made to the Board-approved Cost Allocation methods are appropriate.

D. "End-State" Revenue-to-Cost Ratios

78. After the Board has determined unresolved issues with respect to the Cost Allocation methods Hydro One is to apply, the approved cost allocation methods will be applied to produce revenue-to-cost ratios for the new customer classes

⁵⁷ Argument-in-Chief of Hydro One, Transcript Volume 7, July 22, 2008, pp. 33-35

⁵⁸ Transcript Volume 5, July 17, 2008, pp. 152-161

which the Board approves. CME agrees that, when using the results of applying the approved cost allocation methods to guide the design of the new rates, the revenue-to-cost ratios of the proposed “end-state” rates for the new customer classes should fall within the limits of the ranges which the Board has established as guidelines for such ratios for different customer classes. However, the upper limit of these ranges should not be the ultimate rate design target. Rather, the ultimate revenue-to-cost ratio target should be unity. CME reiterates the submissions it made in the Motion brought by AMPCO to review the Board’s March 19, 2008 Decision with respect to Oshawa PUC Networks Inc.⁵⁹ to the effect that the concept that rates should be cost-based or cost-related means that the revenue-to-cost ratio target of the Rate Design should be unity and that, over time, the revenue-to-cost ratios of rates to all rate classes should gradually progress towards unity.

E. “End-State” Rate Impact Measurement

79. Hydro One confines its measurement of the impacts of the “end-state” harmonized rates it is proposing in this proceeding to their impact on the “average” customer in each rate class. The “end-state” impact on individual customers most adversely affected within each rate class have not been quantified.⁶⁰ This is a matter of major concern to CME.
80. CME’s concerns with respect to the impact of Hydro One’s proposals on individual customers intensified when it was contacted by Mr. Vickers of the Hopper Foundry. In its pre-filed evidence, Hydro One appeared to downplay the impact of its proposals on the Hopper Foundry by stating “... while the third

⁵⁹ EB-2008-0099, Submissions by CME dated May 15, 2008

⁶⁰ Ex.G1-7-2, p. 10; Ex.G1-8-1, p. 1; Ex.G1-8-2

customer will see a significant percentage increase, the total dollar amount is about \$73K per year.”⁶¹

81. As it turns out, the \$73K increase per year is a 300% adverse annual bill impact on the Hopper Foundry which, if approved, will put the Foundry out of business.⁶² This adverse impact primarily arises from Hydro One’s proposal to terminate its interim TOU Program and the rate under which the Hopper Foundry is currently served.⁶³ We address the inappropriateness of this feature of Hydro One’s proposals later in this Argument.
82. The fact that a General Service customer faces a 300% bill impact as a result of Hydro One’s proposals prompted CME to closely question Hydro One about the impacts of its proposals on those customers in each rate class who will be more adversely affected than the “average” customer in each rate class.
83. The evidence from Hydro One’s witnesses, in response to questions from Counsel for CME and the Board Chair, was to the effect that Hydro One has no idea what the “end-state” impacts of its harmonized rate proposals will be on those members of each class. The witnesses modified this evidence when being cross-examined by counsel for CCC.⁶⁴ There is little, if any evidence, which shows the “end-state” annual bill impacts on General Service customers of Acquired Utilities more adversely affected than the average customer in each of the existing General Service rate classes.
84. We submit that Hydro One’s failure to fully analyze and present in evidence the rate and bill impacts of its proposals on those General Service customers in each rate class more adversely affected than the “average” customer in each class is inappropriate.

⁶¹ Ex.G1-9-1, page 2

⁶² Ex.K4.1, K4.2, K6.6; Transcript Volume 6, July 18, 2008, pp. 36-39, 53-54

⁶³ Transcript Volume 6, July 18, 2008, pp. 69-70

⁶⁴ Transcript Volume 4, July 15, 2008, pp. 93, 94 line 7-13, 98 line 12-18; Volume 5, July 17, pp. 64-65

85. The evidence indicates that those most adversely affected are customers of former municipally-owned utilities, which Hydro One has acquired (“Acquired Utilities”).
86. Hydro One justifies the rate increases its harmonization proposals impose on the customers of Acquired Utilities by labelling them as beneficiaries of a cross-subsidy being provided by Legacy customers.⁶⁵ CME questions, and is aware that SEC will be questioning, the appropriateness of a conclusion that customers of Acquired Utilities are beneficiaries of a cross-subsidy, when there is no evidence showing that rates serving customers of Acquired Utilities fail to recover the costs incurred by each of the Acquired Utilities to provide service.
87. Prior to being acquired by Hydro One, the regulated rate levels charged by these utilities were lower than they are currently because the rates did not include a return or profit component. As well, it is likely that the embedded costs of some of the electricity systems acquired by Hydro One were lower than the embedded costs of Hydro One’s primarily rural system.⁶⁶ It should also be recognized that merging rural customers, who are, generally speaking, more costly to serve than clusters of customers in communities, can, in and of itself, shift costs from the rural customers to the clusters of customers in such communities. This will be the result if methods used to allocate costs inadequately distinguish between those customers who are more costly to serve than others.
88. Increases in rates that have occurred since Hydro One acquired these utilities, include a return on assets not previously charged and a proportional allocation of the overall increase in revenue requirement to rate classes based on class revenues rather than allocated costs.⁶⁷ However, there is no evidence showing the extent to which the existing rates of Acquired Utilities would be higher or

⁶⁵ Transcript Volume 4, July 15, 2008, pp. 45-76

⁶⁶ Transcript Volume 4, July 15, 2008, pp. 101-105

⁶⁷ Transcript Volume 4, July 15, 2008, pp. 101-105

lower if the Board-approved allowed return had been allocated to the rates of each Acquired Utility on a stand-alone basis. Without evidence of this nature, it is inappropriate to label customers of Acquired Utilities as beneficiaries of a material cross-subsidy provided by Legacy customers.⁶⁸

89. Customers of Acquired Utilities will be operating from the premise that their existing rates have been approved by the Board and that, as a result, they are just and reasonable rates. The “end-state” rate impacts on the customers of each class most adversely affected by rate harmonization proposals cannot be dismissed or ignored by now labelling them as beneficiaries of a cross-subsidy.⁶⁹ These impacts need to be considered.
90. We submit that a regulator cannot determine whether proposed rates are “just and reasonable” without knowing the rate impacts on individual customers who will be most adversely affected by the proposed rate changes.
91. To be clear, we are not suggesting that Hydro One must conduct an individual customer rate analysis for each of its 1.1M customers.⁷⁰ The focus of the adverse impact analysis we are suggesting is those customers most adversely affected by the rate proposals and, in particular, those customers in each rate class which are more adversely affected by the rate proposals than the average customer in each rate class.
92. A regulator fails to fulfill its public interest mandate if it approves “end-state” rate levels without knowing their impact on those customers in each rate class who will be most adversely affected. It is the impact of proposed rate changes on those most adversely affected which should be the primary determinant of the

⁶⁸ Transcript Volume 4, July 15, 2008, pp. 100-102

⁶⁹ Transcript Volume 4, July 15, 2008, pp. 45-76

⁷⁰ Transcript Volume 4, July 15, 2008, pp. 96-97

appropriate duration of the transition to full-rate harmonization, rather than the impact of such measures on the “average” customer in each rate class.

93. We submit that the appropriateness of Hydro One’s proposed four (4) year transition to “end-state” rate re-balancing cannot be determined without first considering two items. The first of these items is the “end-state” impacts of Hydro One’s proposals on the customers in each rate class who will be more adversely affected than the “average” customer. The second item for the Board to determine is the maximum annual adverse bill impact on individual customers which the Board considers to be reasonable. We address the “end-state” impact item in this part of this Argument. The maximum annual adverse bill impact item is addressed more fully in the Rate Rebalancing Transition section of this Argument.
94. There is no evidence in this case showing either the maximum adverse annual bill impact on the individual customers in each rate class who will be most adversely affected by Hydro One’s proposals, or the total number of customers who will be more adversely affected than the average customer in each rate class. The evidence in Exhibit H Tab 12 Schedule 61, showing percentage impacts on residential customers at different levels of annual consumption, does not reveal the number of residential customers for whom the “end-state” bill impacts exceed 40%; or 50%; or 60%. The information provides the impacts on “average” customers at various levels of consumption. At lower levels of annual consumption the “end-state” impact on the “average” customers can be quite high such as 98.6% in Arkona, 77.1% in Blyth, 95% in Fenlon Falls, 99% in Kirkfield, 95% in North Stormont, 99% in Perth East, 87% in Quinte West, 83% in Ramara, 112% in Thorndale, 108% in Tweed and 122% in Woodville.⁷¹ Within

⁷¹ Ex.H, Tab 12, Sch.61, Attachment B, pp. 4, 7, 12, 14, 19, 20, 21, 24, 25, 26. See also Attachment C where the “end-state” percentage impacts measured by excluding rate riders is shown for the various residential rate classes. In many cases, these rate impacts are over 100% at all levels of consumption and in other cases, the “end-state” rate impacts exceed 100% at the higher levels of consumption.

these sub-classes of “average” customers we do not know either the number of customers affected or the “end-state” percentage bill impact on the most adversely affected customers. For example, while we know that over 150,000 residential customers will be adversely affected by Hydro One’s rate harmonization proposals, we do not know the range of adverse annual bill impacts which the 10,000 most adversely affected customers will experience.

95. There is no evidence from Hydro One comparable to Exhibit H, Tab 12, Schedule 61 pertaining to the General Service rate classes of Acquired Utilities. Except for a brief exchange between one of Hydro One’s witnesses and counsel for CCC,⁷² there is nothing in the record to quantify the “end-state” annual bill impacts of the most adversely affected General Service customers or the number of General Service customers more adversely affected than the average customer in each of the existing General Service rate classes.
96. In these circumstances, we suggest that an assumption must be made with respect to the percentage annual bill impact on those customers most adversely affected by expressing it as a multiple of the percentage bill impact that the proposals have on the “average” customer in each rate class. The multiple that we urge the Board to apply is four (4), so that if the “end-state” impact of the harmonized rates on the “average” customer in a particular customer class is 35%, then the “end-state” impact on those most adversely affected should be assumed to be about 130%.
97. Our rationale for suggesting a multiple of four (4) is as follows:

⁷² Transcript Volume 5, July 17, 2008, pp. 62 to 64

- (a) The evidence indicates that the “end-state” annual bill impact on the “average” customer in each of the existing General Service (“GS”) rate classes of Acquired Utilities ranges between 3.0% and 36.2%;⁷³
- (b) In Ex.G1, Tab 7, Schedule 2, pp. 4 to 10, there are, by our count, about 89 existing GS < 50 and GS > 50 rate classes. Within these 89 rate classes, we count that there are about 52 cases where the impact on the “average” customer in each class exceeds 20%, where the total bill impact is measured based on “Total Bill Including Distribution and Riders”. We count that there are about 13 existing GS > 50 rate classes where the “end-state” impact exceeds 30%;
- (c) The percentage impact on the “average” GS < 50 Customers in Forest is about 23.1% and, for the GS > 50 subset in Forest, the impact is about 16.5%, using “Total Bill Including Distribution and Riders” as the basis of measurement. The annual bill impact on Hopper Foundry is about 300%, which indicates that the multiple of the “average” rate impact to be applied to derive the impact on the customer most adversely affected exceeds 13. However, the “end-state” rate impact on the Hopper Foundry is not entirely attributable to Hydro One’s rate harmonization proposals;
- (d) The evidence from Hydro One witnesses is to the effect that the “end-state” impact on the “average” GS < 50 customers in Quinte West is about 36% and that, for customers with low consumption, the “end-state” percentage impact is about 700%.⁷⁴ This evidence does not help us to understand the number of GS customers in Quinte West who will experience an “end-state” annual bill impact in excess of 60%, for example. There will be customers in Quinte West for whom the “end-state” impact will exceed the impact on the “average” customer in the class but

⁷³ Ex.G1-2-5, p.8, Table 3

⁷⁴ Transcript Volume 5, July 17, 2008, pp. 62 to 64

we do not know the extent to which the “end-state” impact on customers more adversely affected than the “average” customers exceeds 36%.

- (e) Hydro One’s four (4) year transition period proposal implies that there are customers in existing rate classes for whom the “end-state” impact is about four (4) times the impact on the “average” customer in the class.
98. A consideration of this information prompts us to adopt a multiple of four (4) to be applied to the impact on the “average” customer in the GS customer classes to determine the “end-state” impact of those most adversely affected by Hydro One’s proposals.
99. If it is determined that the maximum annual bill impact on any adversely affected customer should be no more than 15%, in the manner described below, then the duration of the transition period can be derived by dividing the “end-state” impact on the most adversely affected customer of 130%, in our illustration, by the maximum annual bill impact on any adversely affected customer of 15% which produces a transition period of 8.7 years. If the Board determines that the maximum annual bill should be greater than 15%, then the duration of the transition period shortens.
100. Findings with respect to the “end-state” bill impacts of the harmonized rate proposals on those members of each class most adversely affected and the maximum annual bill impact the Board accepts as reasonable are essential to a determination of the appropriate rate re-balancing transition period.

F. Rate Re-Balancing Transition

101. The Board’s guidelines upon which Hydro One has relied in developing its rate re-balancing transition proposals accept, as reasonable, an annual bill impact of

no more than 10% on the “average” customer within a customer class.⁷⁵ To our knowledge, the Board has not yet established any tolerance limit for the annual bill impact of a rate increase on individual customers within the customer class who are most adversely affected by the proposed rate changes.

102. We invite the Board to provide guidance with respect to this tolerance limit and suggest that an annual bill impact of 150% of the bill impact on the “average” customer is as much as any utility customer can reasonably be expected to tolerate. We suggest that any utility customers who receive more than a 15% increase in their annual bill, before additional incentive regulation adjustments and other add-ons for “pass-through” items and periodic deferral account clearances, are likely to be very upset.
103. Since Hydro One has failed to provide any evidence of the “end-state” rate impacts and the total number of customers of each class most adversely affected by its rate harmonization proposals, the Board must derive an appropriate rate re-balancing transition period by making an assumption with respect to “end-state” impacts on those members of each class most adversely affected by Hydro One’s proposals.
104. As already noted, the assumption we urge the Board to apply is a multiple of four (4) times the “end-state” impact on the “average” customer in each class. The evidence indicates that, for average customers in the existing Residential customer class of the Acquired Utilities, the “end-state” rate impact on the “average” customer is up to about 31%.⁷⁶ For General Service customers, the “end-state” rate impact on the “average” customer in the existing General Service customer class of Acquired Utilities is about 36%.⁷⁷ Applying a multiple of four (4) to these “end-state” impacts for the “average” customer in each class produces

⁷⁵ 2006 Electricity Distribution Rate Handbook, p. 131

⁷⁶ Ex.G1-7-2, p. 9; Ex.G1-2-5, p. 8; Ex.G2-2-1, p. 15; Transcript Volume 4, July 15, 2008, pp. 105-106

⁷⁷ Ex.G1-7-2, p. 9; Ex.G1-2-5, p. 8; Ex.G2-2-1, pp. 15-16; Transcript Volume 4, July 15, 2008, pp. 105-106

“end-state” impacts for those most adversely affected of 121% in the Residential class and 144% in the General Service class. If, as we suggest, the Board sets the tolerance limit for annual bill impacts on individual customers at 15% (150% of 10%), then the appropriate rate re-balancing transition period for the Residential class is about 8 years and for the General Service class is about 9.6 years. The foregoing is the type of process we urge the Board to apply to determine the appropriate duration of the rate re-balancing transition. If the Board sets the tolerance limit for bill impact at 20% then the transition period for Residential customers will be about 6 years and for General Service customers about 7 years.

105. Mitigation of impact on those most adversely affected should be the primary consideration when determining the duration of the rate re-balancing transition period. Factors such as the duration of rate setting for Hydro One under an IRM or its transition to a new billing system should have no influence on the Board’s determination. Hydro One’s witnesses acknowledged that a transition period greater than 4 years could be accommodated.⁷⁸
106. Another feature of Hydro One’s rate re-balancing transition proposal which we question is the “front-end loading” aspect pursuant to which, the rate impact on the “average” customer in each rate class is capped at 10% for 2008, 8% in 2009, and 7% in 2010. We submit that the percentage impact on an “average” customer in each year should be derived from dividing the rate re-balancing transition duration determined as described herein by the “end-state” bill impact on the “average” customer in each rate class. If the “end-state” bill impact on the “average” customer in a Residential rate class is up to 31% and the duration of the rate re-balancing transition as determined in the manner described above is eight (8) years, then the percentage impact on an “average” customer in each

⁷⁸ Transcript Volume 6, July 18, 2008, pp. 189 to 191

year should be smoothed or equalized to a level of about 4% ($31 \div 8 = 3.88$) for each of the eight (8) years in the rate re-balancing transition period.

107. We submit that there is no good reason for the front-end load feature in Hydro One's rate re-balancing transition proposal. The bill impact cap should be equalized for the entire transition period so that the progress to harmonized rates will be less disruptive for all adversely affected customers in each rate class.

G. Termination of Interim TOU Program

108. All of the rates in Hydro One's rate harmonization proposal presume that Hydro One has an ability to meet the peak period demand of any customer, at any time during the 24 hours in each day. None of the rates contained in Hydro One's rate harmonization proposal are premised on an inability of Hydro One to meet the customer's peak period demands at any time during the 24 hour day. The only "off-peak" rate currently available, which enables Hydro One to confine its peak period service to a particular customer to less than 24 hours in a day, is the "off-peak" rate which forms part of the Interim TOU Program approved by the Board on November 24, 2004.⁷⁹
109. Three (3) customers currently take service under the auspices of Hydro One's Interim TOU Program. Two (2) customers will be better off under the new rate classifications Hydro One proposes. The third, Hopper Foundry, is in a unique situation.⁸⁰
110. Hopper Foundry has been an existing customer of Hydro One and its predecessors for many years.⁸¹ It operates in the evenings.⁸² Hydro One's distribution facilities providing service to the community in which the Hopper

⁷⁹ RP-2004-0203/EB-2004-0457

⁸⁰ Ex.G1-9-1, p. 2

⁸¹ Ex.K4.1

⁸² Ex.K4.1; Transcript Volume 6, July 18, 2008, pp. 28-29

Foundry is located are inadequate to enable Hydro One to satisfy the peak period demands of the Hopper Foundry 24 hours per day. Stated another way, Hydro One can only satisfy its obligation to serve the Hopper Foundry by meeting its peak demand in the off-peak evening period.⁸³

111. Until such time as Hydro One can meet the peak demands of the Hopper Foundry in the daytime, it is inappropriate for Hydro One to ask the Board to impose a rate on the Hopper Foundry which is based on the system-wide costs of providing services to meet their customers' needs at any time during a 24 hour day.⁸⁴ Hydro One currently cannot discharge that 24 hour per day obligation to Hopper Foundry.
112. Until Hydro One has upgraded its distribution system serving Forest to a point that it can meet the peak demands of Hopper Foundry 24 hours a day and thereby discharge its obligation to serve this existing customer under the auspices of a 24 hour per day rate, the off-peak Interim TOU program rate should remain available to Hopper Foundry.
113. Another alternative is to maintain the availability of the off peak interim TOU rate until such time as that rate is replaced with a cost-based rate which limits Hydro One's obligation to meet a customer's peak demands in an off peak period. The rationale for TOU pricing is that the costs of serving a customer's peak demand in an off-peak period are materially less than serving their peak demands during peak periods. In these circumstances, Hydro One's proposal to terminate the interim TOU Program is inappropriate because it operates to force Hopper Foundry, an off peak customer, onto a rate which is based on the costs of serving peak demands during peak periods.

⁸³ Ex.K4.1; Transcript Volume 6, July 18, 2008, pp. 29-30, 39

⁸⁴ Transcript Volume 6, July 18, 2008, pp. 39, 42

114. In addition, Hydro One's proposal to terminate the off peak rate in its interim TOU Program, before a replacement TOU rate is available, is contrary to prevailing public policy. On this ground alone, the Board should reject the proposal and order that the program continues.
115. If Hydro One enhances its system to be capable of meeting Hopper Foundry's peak demands in the daytime hours, then the Hopper Foundry could be transitioned to the 24 hour per day rate class within Hydro One's harmonized rates, which applies to its service. A far better solution is to order the continuance of Hydro One's TOU program until cost-based rates are available to serve customers whose peak demand is confined to an off peak period.
116. The cost consequences of Hydro One's inability to discharge its obligation to serve an existing customer under the auspices of distribution rates which are premised on accommodating that customer's peak demands at any time during a 24 hour day, are the responsibility of Hydro One's shareholder and not its ratepayers. Once Hydro One has upgraded its system to provide it with the capacity to meet a customer's peak demands at any time during the 24 hour day, the cost responsibility for such system upgrades will shift to ratepayers.
117. We submit that, in the context of its impact on the Hopper Foundry, Hydro One's proposal to terminate the Interim TOU Program is incompatible with class ratemaking principles. We suggest that the solutions we have outlined respect class ratemaking principles and, for these reasons, urge the Board to reject Hydro One's proposal to terminate the availability of the TOU rate currently serving Hopper Foundry and two (2) other customers. We urge the Board to direct Hydro One to continue to provide service under the TOU rate until it is either replaced with a cost-based rate which limits Hydro One's obligation to meet the customer's peak period demand in "off-peak" periods, or until such time

as Hydro One has upgraded its system to provide it with the capacity to meet the peak period demand of the Hopper Foundry at any time during the 24 hour day.

IX. DEFERRAL AND VARIANCE ACCOUNTS

118. The new variance accounts OPG asks the Board to approve are as follows:⁸⁵

- (a) Pension Cost Differential;
- (b) OEB Cost Differential; and
- (c) Bill Impact Mitigation.

119. We have discussed with CCC, VECC, and SEC representatives the detailed submissions which they will be making in support of the proposition that the Board should decline to approve the Pension Cost Differential and the OEB Cost Differential Variance Accounts. CME adopts these arguments. We urge the Board to refuse to approve these two (2) new variance accounts for the reasons articulated by counsel for those parties.

120. We urge the Board to approve the Bill Impact Mitigation Account for the purpose of recording therein a fixed amount of \$2.5M which will be cleared in future years. Hydro One's shareholder should not be at risk for this revenue shortfall for the reasons articulated by Hydro One representatives.

121. We submit that issues with respect to the allocation of the amount recorded in the Deferral Account should be addressed at the time Hydro One applies to clear the account. While we accept that the \$2.5M should be recovered from all customers as a system cost, the Board's determination of the appropriate allocation factor for distributing the cost to the various rate classes should be

⁸⁵ Ex.F1-3-1, p. 1

deferred to the proceeding in which Hydro One applies to have the account cleared to ratepayers. At that time, it is likely that disputes with respect to Hydro One's proposed new rate classifications will have been resolved. Alternatives for allocating responsibility for the Bill Impact Mitigation costs should be considered after, and not before, the Board resolves disputes with respect to customer classification.

122. CME has no particular submissions to make with respect to Hydro One's proposal to clear to ratepayers balances in the RSVA account and the Tax Changes deferral account. We rely on the Board to apply its expertise to resolve the issues Board Staff has raised in its submissions with respect to the clearance of the balances in these accounts.

X. COSTS

123. CME requests an award of 100% of its reasonably incurred costs of participating in this proceeding being one of considerable importance to the 1.2M electricity consumers served by Hydro One. The rate harmonization implications of this case could adversely affect many of Hydro One's electricity customers for years. As well, the Board's determination of Hydro One's 2008 revenue requirement and rates will become the base from which Hydro One's rates will be derived for the years 2009, 2010 and 2011 under the auspices of the Board-approved 3rd Generation IRM.
124. Through its counsel, CME actively participated in the Settlement Conference and hearing to assure that the implications of Hydro One's proposals for CME member companies, who take service from Hydro One, are carefully scrutinized. Throughout the process, counsel for CME collaborated with other parties having

similar interests in an attempt to minimize duplication and to enhance the efficiency of the regulatory process.

125. In these circumstances, we respectfully ask the Board to find that our participation in the proceeding was responsible and of assistance to the Board.
126. With respect to the timing of cost award, we request that the Board consider issuing cost awards to eligible intervenors before the final Decision is released. We urge the Board to consider the procedure adopted by the Board Panel hearing the Application of Ontario Power Generation Inc. ("OPG")⁸⁶. In that proceeding, the Board directed eligible intervenors to submit two (2) separate Cost Claims: one covering the period to the close of the evidentiary portion of the hearing, and the other covering services rendered for the remaining duration of the process.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 18th day of August, 2008.



Peter C.P. Thompson, Q.C.
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