Ontario Energy Board
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto ON M4P 1E4
Telephone: 416- 481-1967
Facsimile: 416- 440-7656
Toll free: 1-888-632-6273

Commission de l'énergie de l'Ontario
C.P. 2319
27e étage
2300, rue Yonge
Toronto ON M4P 1E4
Téléphone; 416- 481-1967
Télécopieur: 416- 440-7656
Numéro sans frais: 1-888-632-6273

BY EMAIL

January 12, 2009

Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: Town of Essex
Application for Leave to Acquire Shares of E.L.K Energy Inc. ("ELK")
Board File No. EB-2008-0310

Please see attached Board Staff Interrogatories for the above proceeding. Please forward the attached to the Applicant and all intervenors in this proceeding.

Yours truly,

Original signed by

Judith Fernandes
Case Manager

Board Staff Interrogatories
Town of Essex
Application for Leave to Acquire
Shares of E.L.K Energy Inc. ("ELK")
EB-2008-0310

1. **Valuation of ELK Shares**
   Ref: Section 2.3.1

   In its application, the Town of Essex states that the purchase price offered of $12,773,240 is based on matching a third party offer with no assumptions being made in the valuation about future rate levels.

   a. Please advise the Board of the acquisition premium that is being paid, if any, in the purchase price of the proposed transaction.

   b. Please confirm the Town of Essex's understanding, as per the August 31, 2005 combined MAADs Decision (EB-2005-0234, EB-2005-0254 and EB-2005-0257) and the *Board's Report on Rate-making Associated with Distributor Consolidation* issued July 23, 2007, that any acquisition premium is not normally recoverable in rates.

   c. If the Board approves the transaction, and the transaction is completed, please explain ELK's approach in terms of operating the ELK service area. Specifically, please identify any plans currently known or being planned by ELK for recovery of part or all of any purchase price premium through efficiency gains (e.g. reductions to OM&A).

   d. Please confirm that recovery of any purchase price premium through efficiency gains can be accomplished without impairing ELK's ability to maintain its distribution operations to existing customers (i.e. with risk of service quality or reliability degradation, and appropriate operations and capital expenditures to maintain its existing infrastructure and to make necessary investment for any growth).

2. **Financing of the Share Purchase Transaction**
   Ref: Section 2.3.4

   In its application, the Town of Essex states that the alteration in ELK's capital structure resulting from the bank financing will not impact the financial viability of ELK. Following completion of the transaction, ELK's actual capital (debt/equity) structure is forecasted to change from 40/60 to 78/22 in the first year following the transaction.

   a. Please identify the impacts on ELK's cash flow position going forward with respect to meeting interest and principal payments given the increased debt in its capital structure.

   b. Please explain what impact, if any, the increased debt will have on ELK's ability to attain any third party financing at reasonable rates in the future, should it be required to finance investments in ELK's distribution assets beyond the loan for $3 million to finance ELK's planned investments in smart meters as documented in the loan with the Toronto Dominion Bank.

3. **Loan between ELK and the Toronto Dominion Bank**

   If approved, a condition of closing is that ELK will issue a dividend of $10.6 million to the Town of Essex, which will provide part of the cash by which the Town of Essex is purchasing the shares owned by Lakeshore and Kingsville and debt owed by ELK to Lakeshore and Kingsville. In turn, ELK will raise part of the $10.6 million dividend through a loan with the Toronto Dominion Bank for $8.0 million.

   A copy of the Toronto Dominion Bank loan is provided in Tab I of the Application.

   a. Please identify the source of the remaining $2.6 million of the dividend from ELK (i.e. the portion of the 10.6 million dividend not financed by the loan from the Toronto Dominion Bank).

   b. The loan agreement document states that the loan can be consummated in various forms (fixed rate or floating rate, rate term up to 10 years, amortization up to 20 years). For a fixed rate loan, the rate shall be a set by the Toronto Dominion Bank based on the term selected by ELK. For a variable or floating rate term, the rate is determined to be Bank Prime + 0.0%.

i. Please provide ELK's views of the form of the loan that it expects to take, and the rate.

ii. Given that the $8.0 million loan results in significant leveraging of ELK, please confirm whether the loan rates being negotiated with the Toronto Dominion Bank incorporate any risk premium due to the significant debt leveraging.

c. In approving rates, the Board generally looks at the market conditions in effect at the time of execution in determining if the terms of an affiliate loan and the applicable interest rate are reasonable. For future or variable-rate loans, the Board will look at forecasts of similar rates, and the Board's own cost of capital methodologies for estimating near-term expected rates.

i. Please provide ELK's views on any risk to ELK's financial viability if the Board were to determine that the rate of the Toronto Dominion Bank loan included a risk premium due to the significant leveraging and that premium should not be recoverable from ratepayers.

ii. Please provide ELK's views on any risk to ELK's financial viability that, in the case of a variable-rate loan, the Board's deemed long-term debt rate as calculated in accordance with Appendix A of the December 20, 2006 *Report of the Board of Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors* was lower than the floating rate as documented in the bank loan.

4. **Documents**
Ref: Tabs B and C: Audited Financial Statements for the Town of Essex and ELK Energy Inc.

It appears that the Audited Financial Statements for the Corporation of the Town of Essex for the year ended December 31, 2007 are discussion drafts (due to watermarks shown on the pages of the Essex AFS). Please file copies of the final Audited Financial Statements for the year ended December 31, 2007 for the Corporation of the Town of Essex.