



**EB-2006-0501**

**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 or Orders approving  
or fixing just and reasonable rates and other charges  
for the transmission of electricity commencing  
January 1, 2007.

## **PROCEDURAL ORDER NO. 2**

Hydro One Networks Inc. ("Hydro One" or the "Company") filed an Application, dated September 12, 2006, with the Ontario Energy Board under section 78 of the *Ontario Energy Board Act 1998, S.O. 1998, c.15, Schedule B*. The Board has assigned file number EB-2006-0501 to the Application and has issued a Notice of Application dated October 17, 2006.

At the Issues Conference, held on December 8, 2006, parties agreed to all issues on the draft Issues List save for that of charge determinants, which is item 7.3. Parties could not agree upon the wording of a preamble paragraph to the Issues List ("Issues List preamble"), proposed by Hydro One to address the status of certain findings and observations made in the Hydro One Distribution proceeding (RP-2005-0020/EB-2005-0378) (the 'Distribution decision').

At the Issues Day, held on December 14, 2006, the Board reviewed the non-contested issues and accepted them as listed. The Board determined that charge determinants were within the scope of the issues to be determined in this hearing and that item 7.3 should remain on the Issues List. The Board directed that notice should be given to all transmitters and their customers that this proceeding will deal with the issue of charge determinants.

The Board also reviewed the proposed Issues List preamble which makes reference to Schedule 1. Schedule 1 consists of excerpts of certain findings and observations from the Distribution decision which may be relevant to this application. The Board approved the preamble with amendments, and the attachment of Schedule 1 to the Issues List. Appended to this Order as Appendix "A" and "B" respectively, are the approved Issues List with amended preamble and Schedule 1.

The Board also accepted a request to change the date for the filing of intervenor evidence. Attached as Appendix "C" to this Order is an amended timeline reflecting the new date and the alteration of other dates to accommodate this change.

The Board considers it necessary to make provision for the following procedural matters. Please be aware that further procedural orders may be issued from time to time.

**THE BOARD ORDERS THAT:**

The Issues List for this proceeding, attached as Appendix "A" to this Order, is approved and Procedural Order No. 1 is amended as noted below:

1. Parties who wish information and material from the Company that is in addition to the evidence filed with the Board, and that is relevant to the hearing, shall request it by written interrogatories filed with the Board and delivered to the Company on or before Thursday, January 11, 2007. All interrogatories must identify the relevant Issue by Issue Number in the format as shown by the example attached as Appendix "D". Board staff shall submit interrogatories on Thursday, December 21, 2006. Intervenors are expected to review Board staff interrogatories to ensure they do not duplicate questions.
2. The Company shall file with the Board complete responses to the interrogatories and deliver them to the Intervenors no later than Monday, January 29, 2007.

3. Intervenor and Board staff who wish to present evidence shall file that evidence with the Board and deliver it to the Company and the other Intervenor on or before Wednesday, February 14, 2007. An updated list of Intervenor is attached as Appendix "E".
4. The Company has indicated a desire to file an evidence update on Friday, February 23, 2007 with updated 2006 financial data and updates related to the Integrated Power System Plan (the "IPSP"). To allow for Intervenor and Board staff questions on the update, the Board will convene a transcribed technical conference on Tuesday, March 6, 2007 and if need be, Wednesday, March 7, 2007 in the Board's North hearing room at 2300 Yonge Street, 25th Floor, Toronto at 9:30 a.m.
5. Anyone (Intervenor, Board staff or the Company) who requires additional information related to any Intervenor's filed evidence, which is relevant to the hearing, shall request it by written interrogatories filed with the Board and delivered to the parties on or before Friday, February 23, 2007. Responses to the interrogatories shall be filed with the Board and delivered to the Applicant and the other Intervenor on or before Friday, March 2, 2007.
6. An Intervenor Conference will be convened on Tuesday, March 20, 2007 at 9:30 a.m. Any registered Intervenor in this proceeding may attend. The Intervenor Conference will be held at 2300 Yonge Street, Toronto in the Board's ADR room on the 25th Floor and may continue until Wednesday, March 21, 2007, if needed. The purpose of this meeting is for Intervenor to develop a common proposal, if possible, to present for consideration by the Company.
7. A Settlement Conference will be convened on Monday, March 26, 2007 at 9:30 a.m. with the objective of reaching a settlement among the parties on the issues and/or narrowing the issues to be dealt with at the oral hearing. The Settlement Conference will be held at 2300 Yonge Street, Toronto in the Board's West hearing room on the 25th Floor and if needed, may continue until Friday, March 30, 2007.
8. Any Settlement Proposal arising from the Settlement Conference shall be filed with the Board no later than 5:00 p.m. on Tuesday, April 3, 2007. The

Board will sit on Tuesday, April 10, 2007 at 9:30 a.m. to review any Settlement Proposal.

9. The evidentiary phase of the oral hearing will commence at 9:30 a.m. on Thursday, April 19, 2007 at 2300 Yonge Street, Toronto in the Board's North hearing room. The hearing is currently scheduled for up to 15 hearing days.

All parties shall file their submissions with the Board Secretary, 10 hard copies and one electronic copy in searchable PDF format at [boardsec@gov.on.ca](mailto:boardsec@gov.on.ca) , by 4:00 p.m. on the date indicated, and copy all parties. Parties must also include the Case Manager, Harold Thiessen [harold.thiessen@oeb.gov.on.ca](mailto:harold.thiessen@oeb.gov.on.ca) and Board Counsel, Donna Campbell [donna.campbell@oeb.gov.on.ca](mailto:donna.campbell@oeb.gov.on.ca) on all electronic correspondence related to this case.

**DATED** at Toronto, December 20, 2006.

ONTARIO ENERGY BOARD

*Original signed by*

Kirsten Walli  
Board Secretary

## **APPENDIX "A"**

### **Hydro One Networks Inc. Transmission 2007 and 2008 Rate Case EB-2006-0501**

#### **Approved Issues List**

##### **Preamble:**

The panel in the Hydro One Networks Inc. distribution application (the 'distribution decision') made certain findings and observations that may be relevant to this application. Attached as Schedule 1 to the proposed issues list are excerpts from the distribution decision containing some such findings and observations. The schedule is for informational purposes only. It is not intended that this proceeding involve a re-examination of decisions made by the Board in the distribution case which are fully applicable to the transmission business.

#### **1. ADMINISTRATION (Exhibit A)**

- 1.1 Are the Affiliate Service Agreements still cost effective and efficient in delivering services? Have any changes occurred in these arrangements since the 2006 distribution rates proceeding (RP-2005-0020/EB-2005-0378)? (A1/T8/S2)
- 1.2 Has Hydro One addressed all relevant Board directions from previous proceedings? (A1/T15/S3)?
- 1.3 Is the proposal to establish a revenue requirement beyond the 2007 and 2008 test years without a separate cost of service approval appropriate?
- 1.4 Is the proposed methodology to establish the future revenue requirement beyond 2007 and 2008 appropriate?
- 1.5 Is the proposal to include capital spending as incurred in Rate Base for 2009-2010 appropriate? (A1/T13/S1)
- 1.6 Are Hydro One's Economic and Business Planning Assumptions for 2007 and 2008 appropriate?

#### **2. COST OF SERVICE (Exhibit C)**

- 2.1 Are the overall levels of the 2007 and 2008 Operation, Maintenance and Administration Budgets appropriate? (C1/T1/S1)

- 2.2 Is the 2007 and 2008 budget for Human Resources related costs (wages, salaries, benefits, incentive payments and pension costs) including employee levels, appropriate? (C1/T3/S1&2)
- 2.3 Is the proposed level of corporate O&M costs allocated to the transmission business for 2007 and 2008 appropriate and in line with the O&M cost allocation approved by the Board in Hydro One's 2006 distribution proceeding (RP-2005-0020/EB-2005-0378)? (C1/T5/S1&2)
- 2.4 Is Hydro One's depreciation expense appropriate for 2007 and 2008 and in line with the depreciation methodology approved by the Board in Hydro One's 2006 distribution application (RP-2005-0020/EB-2005-0378)? (C1/T6/S1&2)
- 2.5 Is Hydro One's proposed transmission overhead capitalization rate appropriate? (C1/T5/S2)
- 2.6 Are the amounts proposed to be included in 2007 and 2008 revenue requirements for capital and property taxes appropriate? (C2/T4/S1)
- 2.7 Is the amount proposed to be included in 2007 and 2008 revenue requirements for income taxes, including the methodology, appropriate? (C1/T7/S1)

### **3. RATE BASE (Exhibit D)**

- 3.1 Are the amounts proposed for the 2007 and 2008 Rate Base appropriate? (D1/T1/S1)
- 3.2 Are the amounts proposed for Capital Expenditures in 2007 and 2008 appropriate? (D1/T3/S1&3)
- 3.3 Is Hydro One's corporate asset allocation for the transmission business in line with the common capital and common asset allocation approved by the Board in Hydro One's 2006 distribution application (RP-2005-0020/EB-2005-0378)? (C1/T5/S3) (D1/T3/S5)
- 3.4 Is the proposed inclusion of "Supply Mix" Capital Project expenditures in 2007 and 2008 Rate Base as they are incurred, appropriate? (D1/T1/S4)
- 3.5 Is the submitted Lead Lag study appropriate for the development of the Working Capital component of the Rate Base? (D1/T1/S5)

- 3.6 Does the Asset Condition Assessment adequately address the current condition of the transmission system assets and the determination of capital needs of the system in the future? (D1/T2/S1)
- 3.7 Is the method that Hydro One has used to calculate AFUDC appropriate? (D1/T4/S1)

**4. COST OF CAPITAL/CAPITAL STRUCTURE (Exhibit B)**

- 4.1 What is the appropriate Capital Structure for Hydro One Networks' transmission business for the 2007 and 2008 test years? (B1/T1/S1) (B1/T3/S2)
- 4.2 What is the appropriate Return on Equity (ROE) for Hydro One Networks' transmission business for the 2007 and 2008 test years? (B1/T1/S1) (B1/T3/S2)
- 4.3 Are Hydro One's proposed costs for its debt and preference share components of its capital structure appropriate? (B1/T2/S1)
- 4.4 Should the Capital Structure, Capital Costs and Rate of Return on Equity vary between Hydro One's distribution and transmission businesses? (B1/T3/S1)

**5. REVENUE REQUIREMENT (Exhibit E)**

- 5.1 Is the proposed amount for 2007 and 2008 External Revenues, including the methodology used to cost and price these services, appropriate? (E3/T1/S1)

**6. COST ALLOCATION (Exhibit G)**

- 6.1 Are Hydro One's proposed cost pools appropriate and have the costs assigned to these pools been allocated appropriately? (G1/T1-6)
- 6.2 Is the proposed cost allocation treatment of "dual function" lines appropriate? (G2/T2/S1)
- 6.3 Is it appropriate to create a Wholesale Meter pool and was the establishment of this pool done appropriately? (G1/T5/S1)

6.4 Should the customers directly connected to Network Stations that do not pay Line Connection Charges pay them and if so, what mechanism should be used? (G1/T3/S1)

6.5 To what cost pools should "Local Loops" be allocated? (G1/T3/S1)

## **7. RATE DESIGN and CHARGE DETERMINANTS (Exhibit H)**

7.1 Is the load forecast and methodology appropriate and have the impact of Conservation and Demand Management initiatives been suitably reflected? (A1/T14/S2&3) (H1/T2/S1)

7.2 Have the proposed charge determinants been forecast appropriately for each of the transmission revenue pools? (G1/T1/S1) (H1/T3/S1)

7.3 Is the proposal to continue with the status quo charge determinants for Network and Connection service appropriate? (H1/T3/S1)

7.4 Is it appropriate to continue the Export Transmission Service Tariff and should this tariff be changed? (H1/T5/S1, 2 & 3)

## **8. OTHER ISSUES**

8.1 Is the proposal for the establishment and methodology of Hydro One's 2007 and 2008 Deferral and Variance Accounts appropriate? (F1/T3/S1)

8.2 Is the proposal for the amounts and disposition of Hydro One's existing Deferral and Variance Accounts (Regulatory Assets) appropriate? (F1/T1/S1)

8.3 Has Hydro One delivered an adequate level of service and other performance compared with other jurisdictions and other relevant performance standards? (A1/T15/S1, 2&3)

8.4 Has Hydro One demonstrated the need to reinforce the existing 115kV connection lines between Leaside TS and Birch Junction TS in the city of Toronto project? (D2/T2/S3)



## **RATE IMPLEMENTATION**

- 9.1 How should the Board deal with any revenue implications regarding the Hydro One Transmission earnings/sharing mechanism (EB-2005-0501) established by the Board?
- 9.2 Are the bill impacts as a result of this application for various customer groups reasonable? (A1/T2/S1)

## **APPENDIX “B”**

### **SCHEDULE 1**

#### **LOAD FORECASTING METHODOLOGY**

To order Hydro One to alter or change its proven forecasting methodology, the Board would require convincing expert evidence supporting the need for change. No such evidence was led by any of the intervenors. The use of dummy variables in econometric analysis is a standard tool and its very purpose is indeed to increase the fit of the observed data. The evidence indicated a very minimal variation between forecast loads resulting from the use of the Company's methodology and actual loads in the planning years between 1997 and 2004. Within that reporting period, the weather corrected actual energy consumed was within one standard deviation of the forecast. The Board therefore accepts Hydro One's load forecast of 41,509 GWh for the 2006 test year. [para. 2.2.8, p. 6]

#### **FORECAST CDM**

While intervenor arguments opposing the CDM factor in the load forecast were not based upon sound technical evidence, the problem may well have stemmed from the fact that Hydro One's CDM forecast was established on provincial targets and some estimate of how those targets will influence Hydro One loads. The Board was dissatisfied with the clarity and precision of the determination of the forecast CDM, and expects Hydro One to provide a more sound analysis of CDM program details and reduction objectives in future applications. [para. 2.3.9, p. 8]

The Board agrees that the forecast load reduction due to CDM efforts should be based upon thoughtful expectations of results from a defined CDM program; however, that is not how the reduction was conceived in this case. [para. 2.3.10, p. 8]

The Board also acknowledges that there appears to be an insufficient understanding at this time, of the CDM programs and expected participation to define an LRAM capable of protecting either the ratepayer or the utility. [para. 2.3.11, p. 8]

The Board accepts Hydro One's arguments regarding the complexity of establishing an LRAM at this time. However, the Board is dissatisfied with Hydro One's efforts to evaluate and analyze the quantum of the forecast load reduction due to CDM programs. The Board understands that Hydro One is not in direct control of the load reductions that may result from CDM activities of others, but no other party, except perhaps the OPA, is in a better position to estimate those

effects, and certainly no other party, has a greater interest in doing so. [para 2.3.12, p. 8]

Several parties observed that Hydro One needs to internalize a Conservation Culture and the Board agrees. The Board expects Hydro One to present future CDM load reduction forecasts with a bottom-up analysis estimating the expected results of their CDM activities and those of others that affect their loads. The Board expects Hydro One's next CDM load reduction forecast, of this order of magnitude, to include a proposal for an LRAM. [para. 2.3.13, p. 8]

## **INERGI CONTRACT**

The Board notes that despite considerable scrutiny regarding the Inergi arrangement, intervenors did not identify any concerns regarding the selection process, the terms of the contract and the performance to date. Only CME suggested that benchmarking processes could be improved. It is the Board's assessment that the Inergi contract represents a reasonable strategy by Hydro One to reduce costs, improve efficiencies and improve focus on the utility's primary operations. The Board is satisfied that the cost consequences flowing from the Inergi agreement for the test year are reasonable and therefore approved for ratemaking purposes. [para. 3.3.4, p. 14]

## **COMPENSATION, BENEFITS AND PENSION COSTS**

The Board notes that the high compensation issue for Hydro One has a considerable history before this Board, dating back to the Ontario Hydro days. The Board has noted in this proceeding that since the de-merger of Ontario Hydro, Hydro One has taken a number of steps to control its overall compensation costs by, for example, instituting a voluntary retirement program, outsourcing, use of the PWU hiring hall, initiating various cost efficiency programs, holding the line on compensation increases for management employees and imposing a two-tiered pension structure or a pension plan that is less generous for new employees represented by the Society of Energy Professionals. These are positive steps and the Board expects the company to continue and enhance such efforts in the future and report to the Board at the next main rates case. The Board is particularly concerned about the apparently high labour rates. In this respect, the Board expects Hydro One to identify what steps the company has taken or will take to reduce labour rates. [para. 3.4.3, p. 14]

Even so, the comparisons between Hydro One's cash compensation with certain other utilities presented by intervenors are of concern. For example, SEC calculated that by applying Ottawa Hydro's compensation costs to Hydro One employees there would be a reduction of about \$85 million in Hydro One's cash compensation. The Board recognizes that there may be some roughness in the derivation of that figure and some differences in the profile of the two utilities.

However the contrast between the compensation structures is of concern to the Board. [para. 3.4.4, p.15]

The Board will not make an adjustment to the proposed OM&A costs based on compensation levels at this time but expects the utility to demonstrate in the future that lower compensation costs per employee have been achieved or demonstrate concrete initiatives whereby compensation costs will be brought more in line with other utilities. [para. 3.4.5, p. 15]

VECC noted that none of the \$3.4 million in incentive payments paid to employees have been charged to the shareholder when achievement of target net income is one of the factors in the criteria for incentive pay. While the Board does not consider the achievement of net income to be a factor that works only for the benefit of the shareholder, as customers also benefit by a financially healthy utility through higher credit ratings and good service, the Board would be concerned if this factor predominated compared to the other factors determining incentive pay. The Board expects Hydro One to file appropriate evidence in the next main rates case to establish that none of the incentive compensation should be charged to the shareholder. [para. 3.4.6, pp. 15-16]

VECC also noted that Hydro One includes 50% of bonus payments in the calculation of pensionable earnings and suggested that the shareholder should be responsible for part of this liability. The Board notes from the evidence that approximately one in five government sector companies and half of the non-government sector companies listed in the Mercer database consulted by Hydro One provide this benefit. There are a sufficient number of companies that provide such benefit for the Board to conclude that it is a reasonable practice and the Board will not reduce Hydro One's proposed costs in this regard. [para. 3.4.7, pp. 16]

## **PENSION COSTS**

CME suggested that Hydro One should look into changing its pension plan from defined benefit to a defined contribution type to avoid funding fluctuations. In the Board's view, changes to the type of pension plan selected is a management decision and likely a result of labour negotiations; as such, and given the cursory canvas of the matter in this proceeding, the Board leaves decisions concerning the pension plan to the discretion of Hydro One management. The Board will not provide any direction to the utility at this time. This does not prevent the utility from coming forward on its own accord with any plans that it may have in this regard. [para. 3.4.18, p. 18]

The Board will not reduce Hydro One's proposed pension costs. [para. 3.4.19, p. 18]

## **BENCHMARKING STUDY**

While the Board is not prepared to order a comprehensive benchmarking study, the Board sees value in a high level benchmarking study for initial review at the next rate proceeding. The Board directs Hydro One to engage an independent party to develop a list of comparable North American companies with similar business models (transmission and/or distribution) and to report on high level comparative performance and cost information for Hydro One and these companies. In future rate cases, this information may assist with determination of areas for a more comprehensive benchmarking review. The Board does not anticipate that the high level benchmarking study will be overly costly. The Board anticipates that Hydro One will want to consult with intervenors regarding the scope of the study. The independent study should be submitted as part of Hydro One's next main application for distribution rates. On best efforts basis, Hydro would also submit the report as part of its transmission rates application for 2007. [para. 3.5.6, p. 20]

In addition, the Board directs Hydro One to engage an independent party to develop a comparison of labour rates and overtime policies amongst Hydro One, other comparative Ontario electricity distributors, and other Canadian utilities as identified in the high level benchmarking study. This independent study should also be submitted as part of Hydro One's next main applications for distribution and transmission rates. [para. 3.5.7, p. 20]

## **COST ALLOCATION METHODOLOGY**

The Board notes that all intervenors accepted the Rudden study as a fair and balanced approach to allocate joint costs and the Board agrees with that assessment. [para. 3.6.7, p. 22]

The Board therefore accepts the recommendations contained in the Rudden study and accepts the costs flowing to Hydro One Distribution for purposes of setting 2006 rates. The Board also considers it reasonable for the Company to employ the Rudden methodology in the pending transmission case. As noted by SEC, this should not prevent parties from raising issues that were not raised in this proceeding. [para. 3.6.8, p. 22]

## **DEPRECIATION STUDY**

In its previous revenue requirement rates case (RP-1998-0001), Hydro One was directed to file an independent Depreciation Study with its next revenue requirement application, which it did. The study, performed by Dr. Ron White of Foster Associates Inc., yields depreciation expenses of \$152.3 million in the test year, compared to \$161.2 million using the existing methodology. If Hydro One had used the depreciation rates in the Handbook, the expense for 2006 would be

\$247.4 million. The proposed depreciation rates yield a lower expense of \$8.9 million over the existing rates and \$95.1 million over the Handbook rates. Intervenor had indicated that they would not cross examine on the issue. Therefore, Hydro One was not required and did not produce witnesses to testify to the Depreciation Study. [para. 3.7.1, p. 23]

The Board accepts the costs flowing from the Depreciation Study for purposes of setting rates in the test year. Such approval should not be construed as Board acceptance of each specific recommendation contained in the study or that the study should form the definitive basis for depreciation studies for other electricity distributors. [para. 3.7.2, p. 23]

## **TAXES**

Hydro One's cost of service includes provisions for Payments in Lieu of Income Taxes (PILS), Capital Tax and Large Corporation Tax, all paid to the Province of Ontario. The Company provided its estimates for these tax payments for 2006. No intervenor objected to the Company's estimates. [para. 3.8.1, p. 24]

The Board accepts the Company's method of calculating these tax provisions, subject to any adjustments that may be required arising from the Board's findings on revenue and cost items in this decision. In a communiqué of December 2005, the Board set out the sources of possible changes to the tax provision for 2006, such as changes in income tax rates, and authorized the establishment of a variance account to capture these differences. [para. 3.8.2, p. 24]

## **LEAD/LAG STUDY—WORKING CAPITAL**

Hydro One was directed by the Board to undertake a lead/lag study, and the Board finds that it acted reasonably when it accepted the Navigant study and its methodology, even though that methodology is inconsistent in certain respects with that of the Handbook. [para. 4.1.17, p. 29]

While the Board has concerns about the inconsistencies, the Board finds the Navigant study to be a well-balanced approach that benefits both the ratepayer and Hydro One. The most significant benefit to the ratepayer is a revenue requirement significantly less than that which would be derived by applying the Handbook methodology. [para. 4.1.18, p. 29]

The Board agrees with the intervenors and Board staff that a review of the merits of either methodology, particularly on the issue of the cost elements excluded by one but included by the other is warranted. Such a review will take into account the methodology that has been previously approved by the Board for the natural gas utilities. Following this review, the Board will consider whether the formulaic approach used in the Handbook should be replaced with a revised version of the Navigant methodology for future rate-making purposes. [para. 4.1.19, p. 30]

Similarly, while the Board accepts the exclusion of customer security deposits from the working cash allowance methodology in this case, the appropriateness of the exclusion remains unresolved by this proceeding. The Board may review this question before issuing the next EDR Handbook. [para.4.1.20, p.30]

## **LINE LOSS REDUCTIONS**

The Board finds that Hydro One acted thoughtfully and prudently with respect to delaying the implementation of the total recommendation of the Kinetrics study, to a timeframe beyond this 2006 rate application. The utility provided good reasons why it could not carry forward the incremental line loss reduction investment in the time frame recommended, primarily related to resources and resource management. The Company in reply argument indicated that they would undertake all of the Kinetrics study recommendations as soon as it was feasible to do so. [para. 4.3.9, p. 34]

The Board does accept the submissions of intervenors regarding the expected benefits of the \$4.75 million expenditure and directs Hydro One to include in its next main rates case filing a budget and a work plan to implement all the cost-effective line-loss reduction suggestions contained within the Kinetrics study. If Hydro One concludes that any of the recommendations in the Kinetrics study should not be implemented, it must clearly demonstrate the reasons for that position, and an accompanying budget and work plan for its preferred implementation plan. [para. 4.3.10, p. 34]

## **ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION**

Allowance for Funds Used During Construction (AFUDC) refers to the costs associated with financing the capital projects that have yet to be recognized in rate base. Hydro One Distribution applied to use its calculation of a pre-tax Weighted Average Cost of Capital (WACC) as the rate for AFUDC. This pre-tax rate of 8.9% resulted in \$6.5 million being added to capital expenditures in the test year and therefore rate base. Hydro One calculated the post-tax AFUDC rate at 7.02% but interpreted the Board's 2006 Rate Handbook Report as allowing the use of a pre-tax WACC. [para. 4.4.1, p. 35]

VECC submitted that the use of the term WACC generally refers to an after-tax number. It also referred to the Board's Distribution System Code which states in APPENDIX B Methodology and Assumptions for an Economic Evaluation, page 2: "A discount rate equal to the incremental after-tax cost of capital based on a prospective capital mix, debt, and preference to the cost rates and the latest approved rate of return on common equity." VECC did not provide a methodology for this after-tax calculation; it just referred to the Distribution System Code. The discounted cash flow approach is applicable to determining

contributions from customers, and perhaps in ranking capital proposals. [para. 4.4.2, p. 35]

The Board's 2006 Rate Handbook Report suggests that WACC be used as the AFUDC rate but the report does not indicate whether the rate would be calculated on a pre-tax or on a post-tax basis, or how the calculation would be made. In the absence of a prescribed method in the Rate Handbook, the Board finds it appropriate to adopt the same method used for gas utilities which relates to interest during construction based on forecast actual borrowing costs. These costs, or rates, may have been decided by the Board in the case, or approved as part of a settlement agreement. [para. 4.4.3, p. 35]

The Board therefore directs Hydro One to recalculate the AFUDC using a rate of 6.2%, which is the Company's blended long-term debt rate. In the generic cost of capital review to be held in 2006, the Board may consider an appropriate methodology for the determination of AFUDC. [para. 4.4.4, p. 36]

## **OVERHEAD CAPITALIZATION**

In its original evidence, Hydro One applied for capitalized overhead of \$48.4 million to be added to distribution rate base in the 2006 test year, reflecting a capitalization rate of 17% contained in the Rudden study. Through an update, the capitalization rate was changed to 15.9% resulting in an adjusted \$46.5 million capitalized overhead to be added to rate base. The Applicant noted that, as recommended in the Rudden study, the calculation for overhead capitalization will be done afresh every year, and an appropriate amount will be trued-up in the following year. [para. 4.5.1, p. 36]

No intervenor took issue with the methodology, results or recommendations in the Rudden study or Hydro One's proposals. The Board accepts the cost consequences for the test year flowing from the Rudden study and the study's recommendations and also accepts Hydro One's truing-up proposal as reasonable. [para. 4.5.2, p. 36]



## APPENDIX "C"

### Hydro One Transmission – 2007/2008 Rates Case (EB-2006-0501) Timetable

(Note: this timetable may be amended from time to time as required by the Board)

|    | Event                                      | Date        |
|----|--|-------------|
|    |  | <b>2006</b> |
| 1  | Issue Procedural Order No. 1               | Nov 30      |
| 2  | Issues Conference                          | Dec 7 & 8   |
| 3  | Issues Day                                 | Dec 14      |
| 4  | Procedural Order No. 2 – Issues List       | Dec 20      |
| 5  | Interrogatories to Applicant – Board Staff | Dec 21      |
|    |  | <b>2007</b> |
| 6  | Interrogatories to Applicant – Intervenors | Jan 11      |
| 7  | Interrogatory Responses                    | Jan 29      |
| 8  | Intervenor Evidence                        | Feb 14      |
| 9  | Interrogatories to Intervenors             | Feb 23      |
| 10 | Intervenor IR Responses                    | Mar 2       |
| 11 | Applicant Evidence Update                  | Feb 23      |
| 12 | Transcribed Technical Conference           | Mar 6 & 7   |
| 13 | Intervenor Conference                      | Mar 20      |

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|    |                             |                               |
|----|-----------------------------|-------------------------------|
| 14 | Settlement Conference       | Mar 26 to 30<br>(if required) |
| 15 | File Settlement Proposal    | Apr 3                         |
| 16 | Settlement Proposal Hearing | Apr 10                        |
| 17 | Oral Hearing                | Apr 19<br>(15 hearing days)   |

**APPENDIX “D”**

**Sample Format for Interrogatories**

(Interrogatory Number) 1

Ref: C1/T5/S2

**Issue Number: 2.6**

**Issue:** Is Hydro One’s proposed overhead capitalization rate appropriate?

Please provide a detailed rationale for the overhead capitalization rate applied in the application.

## APPENDIX "E"

### Updated List of Intervenorors

**HYDRO ONE NETWORKS INC.  
Electricity Transmission Rate Change  
EB-2006-00501  
APPLICANT & LIST OF INTERVENTIONS**

**December 20, 2006**

| <b>Applicant</b>        | <b>Rep. and Address for Service</b>   |
|-------------------------|---|
| Hydro One Networks Inc. | Mr. Glen MacDonald<br>Senior Advisor – Regulatory Affairs<br>Hydro One Networks Inc.<br>8 <sup>th</sup> Floor, South Tower<br>483 Bay Street<br>Toronto ON M5G 2P5<br><br>Tel: 416-345-5913<br>Fax: 416-345-5866<br>Email: <a href="mailto:glen.e.macdonald@HydroOne.com">glen.e.macdonald@HydroOne.com</a> |
| Counsel for Applicant   | Mr. D.H. Rogers, Q.C.<br>Rogers, Moore<br>181 University Avenue<br>Suite 1900, P.O. Box 97<br>Toronto ON M5H 3M7<br><br>Tel: 416-594-4500<br>Fax: 416-594-9100<br>Email: <a href="mailto:don.rogers@rogerspartners.com">don.rogers@rogerspartners.com</a>   |

| <b>Intervenors</b>                    | <b>Rep. And Address for Service</b>   |
|---------------------------------------|---|
| 1. Ontario Power Authority<br>("OPA") | Ms. Miriam Heinz<br>Regulatory Coordinator<br>120 Adelaide Street west<br>Suite 1600<br>Toronto, Ontario<br>M5H 1T1<br><br>Tel: 416-9677474<br>Fax: 416-967-1947<br>e-mail <a href="mailto:miriam.heinz@powerauthority.on.ca">miriam.heinz@powerauthority.on.ca</a> |
| 2. TransCanada Energy Ltd.            | Ms. Margaret Duzy<br>Regulatory Affairs<br>TransCanada Energy Ltd.<br>55 Yonge Str. 8th Floor   |

Toronto, Ontario  
M5E 1J4

Tel: 416-869-2180  
Fax: 416-869-2114  
e-mail: [margaret\\_duzy@transcanada.com](mailto:margaret_duzy@transcanada.com)

And

Ms. Patricia Klewchuck  
Regulatory Research Analyst  
TransCanada Energy Ltd.  
450 – 1<sup>st</sup> Street S.W.  
Calgary, Alberta

Tel: 403-920-7168  
Fax: 403-920-2347  
e-mail: [TCE\\_Regulatory@transcanada.com](mailto:TCE_Regulatory@transcanada.com)

3. Energy Probe Research  
Foundation

Mr. David MacIntosh  
c/o Energy Probe  
225 Brunswick Avenue  
Toronto ON M5S 2M6

Tel: 416-964-9223 ext. 235  
Fax: 416-964-8239  
Email: [DavidMacIntosh@nextcity.com](mailto:DavidMacIntosh@nextcity.com)

And

Mr. Thomas Adams  
c/o Energy Probe  
225 Brunswick Avenue  
Toronto ON M5S 2M5

Tel: 416-964-9223 ext. 239  
Fax: 416-964-8239  
Email: [TomAdams@nextcity.com](mailto:TomAdams@nextcity.com)

4. Consumers Council of Canada  
(the "Council")

Mr. Robert B. Warren  
WeirFoulds LLP  
Barristers & Solicitors  
The Exchange Tower  
Suite 1600, P.O. Box 480  
130 King Street West  
Toronto ON M5X 1J5

Tel: 416-365-1110  
Fax: 416-365-1876  
Email: [rwarren@weirfoulds.com](mailto:rwarren@weirfoulds.com)

And

Ms. Julie Girvan  
2 Penrose Road  
Toronto ON M4S 1P1

Tel: 416-322-7936  
Fax: 416-322-9703  
Email: [jgirvan@ca.inter.net](mailto:jgirvan@ca.inter.net)

5. Association of Major Power  
Consumers in Ontario  
("AMPCO")

Mr. Adam White  
President, AMPCO  
595 Bay Street  
Suite 1201, P.O. Box 69  
Toronto, ON M5G 2C2

Tel.: 416-260-0225  
Fax: 416-260-0442  
E-mail: [awhite@ampco.org](mailto:awhite@ampco.org)

And

Mr. J. Mark Rodger  
Partner  
Borden Ladner Gervais LLP  
Scotia Plaza, 40 King Street West  
Toronto, ON M5H 3Y4

Tel.: 416-367-6190  
Fax: 416-361-7088  
E-mail: [mrodger@blgcanada.com](mailto:mrodger@blgcanada.com)

And

Wayne Clark, P.Eng.  
SanZoe Consulting, Inc.,  
25 Priest Ave.,  
Minesing, Ont.  
L0L 1Y3

Phone: 705.728.3284  
Cell: 705.795.7823  
Fax: 705.721.0974  
E-mail: [wayne.clark@xplornet.com](mailto:wayne.clark@xplornet.com)

6. Coral Energy Canada Inc.  
a Shell Trading Company

Mr. Paul Kerr  
Coral Energy Canada Inc.  
Shell Trading Company  
60 Struck Court, Suite 100  
Cambridge, Ontario  
N1R 8L2

Tel: 519-620-7712  
Fax: 519-624-7712  
E-mail: [Paul.kerr@shell.com](mailto:Paul.kerr@shell.com)

7. Enersource Hydro Mississauga

Mrs. Kathi Litt  
Acting Manager, Rates and Regulatory  
Enersource Hydro Mississauga Inc.  
3240 Mavis Road  
Mississauga, ON  
L5C 3K1

Tel: 905-283-4247  
Fax: 905-566-2737  
E-mail: [klitt@enersource.com](mailto:klitt@enersource.com)

8. Hydro Ottawa Limited

Ms. Lynne Anderson  
Director, Regulatory Services  
Hydro Ottawa Limited  
3025 Albion Road North  
P.O. Box 8700  
Ottawa ON K1G 3S4

Tel: 613-738-5499 ext. 527  
Fax: 613-738-5485  
E-mail: [lynneanderson@hydroottawa.com](mailto:lynneanderson@hydroottawa.com)

9. Vulnerable Energy Consumers  
Coalition ("VECC")

Mr. Michael Buonaguro  
Counsel for VECC  
c/o Public Interest Advocacy Centre  
34 King Street East, Suite 1102  
Toronto ON M5C 2X8

Tel: 416-767-1666  
Fax: 416-348-0641  
E-mail: [mbuonaguro@piac.ca](mailto:mbuonaguro@piac.ca)

And

Mr. Bill Harper  
Econalysis Consulting Services  
34 King Street East, Suite 1102  
Toronto ON M5C 2X8

Tel: 416-348-0193  
Fax: 416-348-0641  
Email: [bharper@econalysis.ca](mailto:bharper@econalysis.ca)

10. Toronto Hydro Electric System  
Limited

Mr. Colin J. McLorg  
Manager  
Regulatory Affairs  
Toronto Hydro-Electric System Limited  
14 Carlton Street  
Toronto ON M5B 1K5

Telephone: 416.542.2513  
Facsimile: 416.542.2776  
email: [regulatoryaffairs@torontohydro.com](mailto:regulatoryaffairs@torontohydro.com)

11. Power Workers' Union ("PWU")

Mr. Bob Menard  
Staff Officer, President's Office  
Power Workers' Union  
244 Eglinton Avenue East  
Toronto ON M4P 1K2

Tel: 416-322-2441  
Fax: 416-481-7914  
Email [rmenard@pwu.ca](mailto:rmenard@pwu.ca)

And  
Mr. Bayo Kidane  
Consultant  
Elenchus Research Associates  
34 King Street East, Suite 600  
Toronto, Ontario M5C 2X8

Tel: 416-348-0666  
Fax: 416-348-9930  
E-mail: [bkidane@era-inc.ca](mailto:bkidane@era-inc.ca)

And  
Ms. Judy Kwik  
Senior Consultant  
Elenchus Research Associates (ERA)  
34 King Street East, Suite 610  
Toronto ON M5C 2X8

Tel: 416-348-9917 ext. 31  
Fax: 416-348-9930  
Email: [jkwik@era-inc.ca](mailto:jkwik@era-inc.ca)

And  
Mr. Richard Stephenson  
Counsel  
Paliare Roland Rosenberg Rothstein LLP  
Barristers  
250 University Avenue, Suite 501  
Toronto ON M5H 3E5

Tel: 416-646-4325  
Fax: 416-646-4335  
Email: [richard.stephenson@paliareroland.com](mailto:richard.stephenson@paliareroland.com)

12. Society of Energy Professionals (SEP)  
Mr. Richard Long  
Legal Counsel  
The Society of Energy Professionals  
IFPTE Local 160, AFL-CIO, CLC  
425 Bloor Street East, Suite 300  
Toronto ON M4W 3R4

Tel: 416-979-2709 ext. 2255  
Fax: 416-979-5794  
Email: [Longr@Society.on.ca](mailto:Longr@Society.on.ca)

13. Gerdau Ameristeel Corporation  
Mr. Darren MacDonald  
Director of Energy  
Gerdau Ameristeel Corporation  
Hopkins Street South  
Whitby, ON L1N 5T1

Tel.: 905-665-3730  
Fax: 905-665-3715  
E-mail: [dmacdonald@gerdauameristeel.com](mailto:dmacdonald@gerdauameristeel.com)

And  
Mr. Shane Freitag



Partner  
Borden Ladner Gervais LLP  
Counsel to Gerdau Ameristeel Corporation  
Scotia Plaza, 40 King Street West  
Toronto, ON M5H 3Y4

Tel.: 416-367-6137  
Fax: 416-361-7392  
E-mail: [sfreitag@blgcanada.com](mailto:sfreitag@blgcanada.com)

14. Independent Electricity System  
Operator (IESO)  
Late intervenor

Mr. David Short  
Senior Regulatory Analyst  
Independent Electricity System Operator  
655 Bay Street, Suite 410  
P.O. Box 1  
Toronto, Ontario  
M5G 2K4

Tel: 905-403 6943  
Fax: 905-855 6129  
E-mail: [david.short@ieso.ca](mailto:david.short@ieso.ca)

And

Mr. John M. Rattray  
Senior Legal Counsel  
Independent Electricity System Operator  
655 Bay Street, Suite 410  
P.O. Box 1  
Toronto, Ontario  
M5G 2K4

Tel: 416-506 2856  
Fax: 416-506 2843  
E-mail: [john.rattray@ieso.ca](mailto:john.rattray@ieso.ca)

15. School Energy Coalition (SEC)  
Late Intervenor

Mr. Bob Williams,  
Co-ordinator  
School Energy Coalition:  
Ontario Education Services Corporation  
c/o Ontario Public School Boards Association  
439 University Avenue, 18th Floor  
Toronto, ON  
M5G 1Y8

Phone: 416-340-2540  
Fax: 416-340-7571  
E-mail: [bwilliams@opsba.org](mailto:bwilliams@opsba.org)

And

John De Vellis  
Counsel - School Energy Coalition's  
SHIBLEY RIGHTON LLP  
Barristers and Solicitors  
250 University Avenue, Suite 700  
Toronto, Ontario, M5H 3E5

Phone: 416 214-5232  
Fax: 416 214-5432  
E-mail: [john.devellis@shibleyrighton.com](mailto:john.devellis@shibleyrighton.com)

And

Rachel Chen  
Principal Consultant  
School Energy Coalition's case manager/consultant  
Institutional Energy Analysis, Inc  
250 University Avenue, Suite 700  
Toronto, Ontario, M5H 3E5

Tel: 416 214-5218  
Fax: 416 214-5418  
E-mail: [rachel.chen@ieai.ca](mailto:rachel.chen@ieai.ca)

16. Ontario Power Generation Inc.  
("OPG")

Andrew Barrett  
Vice President  
Regulatory Affairs and Corporate Strategy  
Ontario Power Generation Inc.  
700 University Avenue, H18-E1  
Toronto, Ontario  
M5G 1X6

Tel: 416-592-4463  
Fax: 416-592-8519  
E-mail: [andrew.barrett@opg.com](mailto:andrew.barrett@opg.com)

Mr. Tony Petrella  
Senior Advisor – Regulatory Affairs  
Ontario Power Generation Inc.  
700 University Avenue, H18-E1  
Toronto, Ontario  
M5G 1X6

Tel: 416-592-3036  
Fax: 416-592-8519  
E-mail: [tony.petrella@opg.com](mailto:tony.petrella@opg.com)

And

Ms. Josie Erzetic  
Solicitor  
Ontario Power Generation Inc.  
700 University Avenue, H18-E1  
Toronto, Ontario  
M5G 1X6

Tel: 416-592-5885  
Fax: 416-592-1466  
E-mail: [j.erzetic@opg.com](mailto:j.erzetic@opg.com)

17. Great Lakes Power ("GLP")  
Late Intervenor

Mr. Viggo Lundhild  
Great Lakes Power Limited  
2 Sackville Road  
Sault Ste. Marie, On  
P6B 6J6

Tel: 705-941-5661  
Fax: 705-941-600  
E-mail: [vlundhild@glp.on.ca](mailto:vlundhild@glp.on.ca)

And

Charles Keizer  
Ogilvy Renault LLP  
Suite 3800  
Royal Bank Plaza, South Tower  
200 Bay Street  
P.O.Box 84  
Toronto, On M5J 2Z4

Tel: 416-216-2342  
Fax: 416-216-3930  
E-mail: [ckeizer@ogilvyrenault.com](mailto:ckeizer@ogilvyrenault.com)

18. The Association of Power  
Producers of Ontario (APPrO)  
Late intervenor

Mr. Tom Brett  
Counsel for the Association of Power Producers of  
Ontario  
Gowling Lafleur Henderson LLP  
Barristers & Solicitors  
Suite 1600  
1 First Canadian Place  
100 King Street West  
Toronto ON M5X 1G5

Tel: 416-862-7525  
Fax: 416-862-7661  
E-mail: [tom.brett@bowlings.com](mailto:tom.brett@bowlings.com)